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~~1464~~ No. 4684 1458  
IN THE  
**United States Circuit Court of Appeals**  
For the Ninth Circuit

BETHLEHEM SHIPBUILDING CORPORATION, LTD.  
(a corporation),

*Third Party Respondent and Appellant,*

VS.

PACIFIC MAIL STEAMSHIP COMPANY

(a corporation),

*Respondent and Appellee,*

JOSEPH GUTRADT COMPANY (a corporation),

*Libelant and Appellee.*

**BRIEF ON BEHALF OF APPELLANT.**

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**FILED**

**NOV 14 1925**

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JOSEPH GUTRADT COMPANY (a corporation),

*Libelant and Appellee.*

---

**BRIEF ON BEHALF OF APPELLANT.**

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**STATEMENT OF FACTS.**

On the 8th day of October, 1923, the Pacific Mail Steamship Company, respondent and appellee above named, hereinafter called the Pacific Mail Company, and the Bethlehem Shipbuilding Corporation, Ltd., third party respondent and appellant above named, hereinafter called the Bethlehem Corporation, entered into a contract, whereby the latter agreed, among other things, to repair the former's vessel, the Steamship "Ecuador," in the following

particulars. (Pacific Mail Company's petition, specifications of contract, items 1 to 11, inclusive. Apos. pp. 17, 18.)

#### "DECK DEPARTMENT.

1. Move ship from Pier 46 to Drydock and after work is completed move ship to Pier 44 or any other Pier designated by owner.

2. Drydock ship.

3. Furnish necessary labor to clean and paint entire bottom to deep load line. One coat of GG Anti-corrosive #1 to deep load line; one coat of GG Anti-fouling #2 to light load line and one coat of boottopping #17. Also letter draft marks forward and aft. (PMSS.-Co. to supply paint.)

4. Overhaul all clapper-valves on ship's sides, renewing all missing or broken pins and clapper-valves (about 30 valves).

5. Raise rudder and renew button under heel pintle  $\frac{3}{4}$ " steel disc.

6. Bore out 1 gudgeon and renew bronze bushing lined with lignum vitae. Renew zinc slabs on rudder arch as found necessary.

7. Quote price per lb. for renewing zinc plates around stern frame.

#### ENGINE DEPARTMENT.

8. Open up main circulating pump, clean out casing and main injection compartment and paint with 2 coats anti-fouling paint.

9. Open out all sea valves in eng. room, grind in seats, repack glands clean and paint chests and strainers and replace valves. (17)

10. Supply lights while ship is in drydock.

11. Draw tail-shaft for examination by Lloyds Surveyor, U. S. Steamboat Inspector, renew lignum vitae in lower half of bearings,



replace and couple up same complete in every detail."

The vessel was delivered to the Bethlehem Corporation on the following day, and redelivered by that corporation to the Pacific Mail Company on the 11th day of October, 1923, as provided in the contract. (Pacific Mail Company's petition, Apos. p. 20.)

On the 13th day of that month the Pacific Mail Company entered into a contract of affreightment with the Joseph Gutradt Company, the libelant and appellee herein, under the terms of which the Pacific Mail Company acknowledged receipt of 1334 cases of salt-water soap in apparent good order and condition, and agreed with the Joseph Gutradt Company, in consideration of the freight charges to be paid to the Pacific Mail Company, to transport said merchandise to Norfolk, Va., and to deliver it there in like apparent good order and condition. (Pacific Mail Company's answer to libel. Apos. pp. 9, 10. Libelant's Exhibit No. 5.)

The remaining facts will be stated with proper references in later portions of this brief. Generally, they are as follows:

On the redelivery of the vessel to the Pacific Mail Company her cargo holds were inspected by the first officer and other deck officers of the vessel, and the loading of cargo was then started. While cargo was being stowed in the 'tween-deck of No. 2 hold the stevedores noticed that the bonnet was off of

the clapper-valve located in the forward part of the 'tween-deck on the port side. This was called to the attention of the first officer, who had the chief engineer bolt the bonnet back in its place. An attempt was made by both of those officers to examine the two other clapper-valves in the 'tween-deck of No. 2 hold, but they were unable to do so by reason of the fact that the 'tween-deck was partially filled with cargo. No attempt was made, however, to remove any part of the cargo in order to get at the other two valves. An inspection was thereupon made of the other holds by the officers of the vessel, and such clapper-valves as were not covered by cargo were examined and found in order.

The vessel started on her voyage from San Francisco at 10:20 P. M., on the night of October 13, 1923, and on the following night at 10 o'clock it was found that the water in the port bilge of No. 2 hold was within a few inches of the cargo in that hold; there being some thirty-five inches of water in the port bilge. The main line engine pump was put on that bilge and at about 11:00 it sucked air indicating that the bilge was dry. At midnight the sounding previously ordered by the master showed the bilge had filled again to the extent of twenty-five inches. There is testimony in the record that other soundings were taken after midnight, and that at 6 o'clock of the following morning a carefully checked sounding showed that there were about twenty feet of water in No. 2 hold.

On arrival of the vessel at the port of Wilmington, the first port of call, later in the morning it was found that the libelant's cargo, together with other cargo stowed in No. 2 and No. 3 holds of the vessel, had been damaged by sea water. On removal of the cargo it was found that at least some of the sea water then in the two holds entered through a clapper-valve in the starboard side aft of the 'tween-deck of No. 2 hold, on which clapper-valve the Bethlehem Corporation had failed to replace a bonnet. The Pacific Mail Company claims that such failure caused the breach of the Pacific Mail Company's contract with the libelant to deliver the latter's cargo in good order and condition. (Pacific Mail Company's petition, Apos. pp. 21, 22, 23.) Hence, the claim that the Bethlehem Corporation is liable to it for the damage for which the Pacific Mail Company is liable to libelant for its breach of the contract of affreightment. (Pacific Mail Company's petition, p. 24.) And the District Court erroneously so held.

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### ARGUMENT.

1. **The Damages Claimed For Injuries to Cargo Were Special Damages, and Not Recoverable Under the Evidence in this Case.**

The Pacific Mail Company alleges in its petition (Apos. p. 15) that it entered into a contract with the Bethlehem Corporation for the repair and overhauling of the S. S. "Ecuador" and the terms of



the contract are then set out verbatim. It further alleges (Apos. p. 20) that the Bethlehem Corporation breached the contract, in that, it redelivered the vessel to the Pacific Mail Company with the bonnets on a number of clapper-valves in No. 2 hold loose, unbolted and improperly fastened. That the Pacific Mail Company relied on the agreement of the Bethlehem Corporation to perform the terms of the said contract, and that in consequence and for that reason stowed cargo in No. 2 hold, and other holds of the vessel. (Apos. pp. 21, 22.) That if the Pacific Mail Company is liable to the libellant for the damaged cargo, then the Pacific Mail Company is entitled to be reimbursed by the Bethlehem Corporation for the damages so paid by reason of the latter's breach of the contract with the Pacific Mail Company, "on account of which breach and not otherwise, the damage to the cargo of Joseph Gutradt occurred." (Apos. p. 24.)

The District Court found in its opinion, in reference to its being a suit upon a contract, and the damages caused by its breach, as follows (Apos. p. 787):

"This is a suit in admiralty in which the libellant seeks to recover damages from the Pacific Mail Steamship Company for breach of a contract of carriage, said respondent in turn, in case it should be held liable. praying judgment against Bethlehem Shipbuilding Corporation, Ltd., on the ground that said damage, if any, arose from the breach by said shipbuilding company of a contract for repairs to the vessel engaged in such carriage.

"On October 8, 1923, the Pacific Mail Steamship Company and the Bethlehem Shipbuilding Corporation, Ltd. (hereinafter referred to respectively as the steamship company and the shipbuilding corporation), entered into a contract whereby the latter agreed to drydock the S. S. 'Ecuador,' owned by the former, to make a number of specified repairs thereto, including overhauling all clapper-valves on the ship's sides, renewing all missing and broken pins and clappers, and to return the ship ready to receive cargo.

\* \* \* \* \*

"The contention of the third party respondent (the shipbuilding corporation) that the damages to the cargo were special in that they could not reasonably have been contemplated by the parties from a breach of the contract for repairs to the vessel, and therefore not recoverable, is untenable. General damages are those which naturally, probably and usually ensue from a failure of performance. The breach here complained of was the failure of the shipbuilding corporation to properly secure or fasten certain underwater clapper-valves. That concern knew that the vessel was largely a cargo carrier; indeed, by the terms of its contract the ship was to be returned to its owner 'ready to receive cargo.' There is no room for argument but that the reasonable and probable, if not inevitable, result of the negligence in question would be serious damage to almost any kind of merchandise stowed in the proximity of the defective valve. The breach of the contract was the efficient cause of the damage."

The burden is upon the Pacific Mail Company to prove that the damages claimed by it are legal damages, and to prove facts which would warrant re-

covery of such damages from the Bethlehem Corporation for the breach of its contract to repair the vessel.

The following testimony was offered by the Bethlehem Corporation on pages 756 and 757 of the Apostles, to which an objection was sustained.

"Mr. LILLICK. In order that the record may have in it what we propose to prove by this witness and in order that the ruling may be made definitely, we propose to prove by this witness that he signed this bid for these repairs for the figure mentioned in it without discussing any of the clauses of the contract, or any of the clauses of the tender for bids with anyone from the Pacific Mail Steamship Company; that this witness knew nothing about the cargo the Pacific Mail Steamship Company proposed to load in the 'Ecuador,' nor upon what voyage the 'Ecuador' was to proceed when she did leave San Francisco after the repairs that were asked for were completed; that in particular the witness had no discussion with any representative of the Pacific Mail Steamship Co. in reference to the clause in the advertisement for bids with the specifications attached, 'Repairs as specified are to be completed on or before 12 o'clock noon October 12, 1923, to the entire satisfaction of our superintendent engineer or his representative'; and the note appended thereto: 'Note. In the award of contract, no specification will be given to possible earlier completion dates. All repairs that would interfere with loading of cargo must be finished and vessel available for loading berth not later than 8 A. M. October 11, 1923; vessel will be ready to go on drydock on or about 8 A. M. October 9, 1923; all work to be finished and vessel alongside Pier 44 or any other pier designated by



the P. M. S. S. Co. and ready to load cargo by 6 o'clock A. M. October 11, 1923.'

"And also that this witness knew nothing about any contracts that the Pacific Mail Steamship Company at that time had with reference to cargo to be carried upon the vessel."

It was not intended by the offer to admit that the burden was upon the Bethlehem Corporation to establish the negative of such a proposition; the sole purpose of the offer was to show good faith on our part and to give the Pacific Mail Company an opportunity to offer evidence, if possible, under which the damages claimed by it might be collected. Also, to prevent the Pacific Mail Company from arguing that the point in reference to the proper rule of damage was merely an after-thought; that it never was an issue during the trial, and consequently the Pacific Mail Company never had an opportunity to offer any evidence on that point.

In the following argument we have purposely omitted any reference to cases on damages which were tort actions (there are none squarely in point). In such actions the rule of damage is more liberal, and necessarily so, because the plaintiff is unable to protect himself by insisting upon having terms in the contract for his protection. A cause of action in tort is much more difficult to establish than a cause of action for a breach of a contract, because it is more difficult to prove negligence. But damages are more easily proved, because of the more

liberal damage rule in tort causes of action. On the other hand a breach of contract is more easily established, but the rule of damage in actions *ex contractu* is much more strict, as will hereinafter more fully appear.

The Pacific Mail Company has not contended, and we assume that it will not, that a party may bring an action for a breach of contract, then after the trial claim that it might have brought an action for the breach of a duty imposed by law and collect damages under the *ex-dilicto* rule of damage established for actions brought originally in tort. This observation will be more clearly understood by reversing the situation and assuming that the Bethlehem Corporation, at the trial, took the position that while it breached its contract, as alleged, still it ought not to be held liable for any damages because it had not been guilty of negligence. It would not be expected of the Pacific Mail Company to admit in such a case that if the defense were proved, it would be a valid defense to its action for a breach of the contract.

The issue here is, were the damages claimed, such damages as the law will allow under the circumstances for the breach of the contract to repair the vessel. In cases *ex contractu*, such as this, the damages allowed may be either general or special, and as different rules are applicable to those classes, it becomes necessary to determine within which classi-

fication come the damages claimed in the present case for injuries to cargo.

The distinction between general and special damages is pointed out in the case of *Howard Supply Co. v. Wells*, (C. C. A.) 176 Fed. 515, where the court says that the former are such damages as the law implies or presumes from the breach complained of, while the latter are such as have proximately resulted but do not always immediately result from the breach and will not, therefore, be implied by law, citing *Lawrence v. Porter*, (C. C. A.) 63 Fed. 62 and *Lillard v. Kentucky Distilleries*, (C. C. A.) 134 Fed. 168, 177.

In *Occidental Mining Company v. Comstock Company*, 125 Fed. 294, the court refers to general damages as those which are necessarily occasioned by the breach, and in *Dissette v. Dost*, 280 Fed. 455, special damages are described as follows:

"If all of the acts by plaintiff complained of by defendant might have occurred without causing any injury to defendant, the damage, if any, to the defendant was special: that is, such damage as is the natural but not the necessary consequence of the act complained of." Citing *Roberts v. Graham*, 18 L. Ed. 791.

To put it differently, general damages are those certain damages which, in a given class of contract actions, it is so apparent that they were the necessary result of the breach that the law presumes, in each case falling within the given class, that those damages were suffered. It may happen, however,



in some cases, that the breach not only caused those damages which the law would imply, but also caused other damages which, although a natural result under the circumstances, do not necessarily result from such a breach. They were a possible but not a necessary result.

To illustrate: A seller fails to deliver a milling machine which the buyer had purchased to make flour at his mill. The general damage which the law implies is the difference in market value between the time when the machine should have been delivered and the contract price, because it will be presumed that in case of failure to deliver the buyer would purchase a machine in the open market from others, hence the difference paid in the market price and the contract price is the necessary result of the buyer's breach. It may happen, however, that the buyer needed the machine at the time that it should have been delivered, in order to run his mill, and while he was attempting to locate another similar machine in the market the wheat which he had on hand spoiled.

There can be no doubt that the seller's failure to deliver the machine was the cause of the loss of the wheat in the sense that such a result from a breach of that kind is well within the range of possibilities, and it was, in fact, the efficient cause in the chain of causations. But the law does not regard that failure as the proximate cause, because such damages were not the necessary consequences of the breach.

They are, then, special damages, and in order to collect them it must be proved that the seller had notice that such special damages would result from a breach *at the time that the contract was made*. As will appear in the cases cited subsequently, not only must notice of special damages be given at the time, but it must be brought home to the party, sought to be charged, in such a manner that it will appear that the liability for special damages was accepted by him *as a condition of the contract*.

Now the question arises, what damages will the law presume would necessarily result from the breach of a contract to repair a vessel? If there was a total failure on the part of the Bethlehem Corporation to make any repairs, no doubt it would be presumed that the Pacific Mail Company would take the vessel to some other shipbuilding company. It would not certainly be presumed that the Pacific Mail Company would take the vessel to sea and then attempt to charge the Bethlehem Corporation for its value if she sank by reason of her unseaworthiness. If incomplete repairs were made by the Bethlehem Corporation, still it could not be presumed that the Pacific Mail Company would send the vessel to sea, but instead would demand that the Bethlehem Corporation complete the repairs and put the vessel in the condition called for by the contract; and if the Bethlehem Corporation refused to do so, the Pacific Mail Company would have it done by another shipbuilding company and charge the

difference in cost to the Bethlehem Corporation, including, probably, the value of the use of the vessel during that time. These costs and value would be the general damages, and the authorities so hold.

In an action for the breach of a contract, in that it was not completely performed or defectively performed, the damage allowed as general damage is the cost of completing the contract or remedying the defect, if it can be done, in order to make the thing done comply with the specifications of the contract.

In *Stillwell Manufacturing Co. v. Phelps*, 130 U. S. 520, 32 L. Ed. 1035, the action was brought for payment of the balance due on a contract whereby plaintiff agreed to furnish and put in complete operation for the defendant, in his flour mill, a seventy-five barrel capacity roller. The defendant set up a counterclaim by reason of alleged defects in the manufacture and design of the machinery furnished. Defendant also claimed damages for delay and for injury to his business. The plaintiff took the position that the defendant, having received the machinery and retained it, bound himself to pay the whole contract price. The court observed, however, that this was not a sale of the machinery subject to the condition that it should be satisfactory to the purchaser, but was an agreement to furnish machinery of a certain description and quality and to set it up and put it in complete operation in defendant's mill. The court then stated the rule of



damages governing such a case as follows, on page 1037:

“The rule of damages adopted by the court below, of deducting from the contract price the reasonable cost of altering the construction and setting of the machinery so as to make it conform to the contract, is the only one that would do full and exact justice to both parties and is in accordance with the decisions upon similar contracts. *Benjamin v. Hillard*, 64 U. S. 23 How. 149 (16:518); *Florida R. Co. v. Smith*, 88 U. S. 21 Wall. 255 (22:513); *Marsh v. McPherson*, 105 U. S. 709, 717 (26:1139), *Cutler v. Close*, 5 Car. & P. 337; *Thornton v. Place*, 1 Mood. & Rob. 218; *Allen v. Cameron*, 3 Tyrwh. 907; S. C. 1 Crompt. & M. 832.”

In *Pullman Palace Car Co. v. Metropolitan Street R. Co.*, 157 U. S. 94, 39 L. Ed. 632, the action was brought by the car company to recover from the railway company a balance alleged to be due for the construction of cars. The cars, when delivered, had insufficient brakes and with those brakes they were useless to the defendant company, which attempted to rescind the agreement. The court found that the position of the defendant in regard to the brakes was well taken, but stated the rule of damage as follows, on page 639:

“If, at trifling expense or without unreasonable exertions, the defendant could have supplied the cars in question with other brakes that were sufficient, the utmost that under all the circumstances it could claim, in reduction of the amount it agreed to pay for the cars, would be the reasonable cost of obtaining new brakes adapted for use on such cars. Stillwell

& B. Mfg. Co. v. Phelps, 130 U. S. 520, 527 (32:1035, 1037); Miller v. Mariners Church Trustees, 7 Me. 51, 20 Am. Dec. 341; Davis v. Fish, 1 G. Greene 407, 48 Am. Dec. 387; Sedgwick, Damages (6th Ed.) 106, 107."

The plaintiff was given judgment for the contract price of the cars, less the amount it would cost defendant to replace the brakes, with other brakes sufficient for the cars.

*Marsh v. McPherson*, 105 U. S. 709, 26 L. Ed. 1139, on page 1142:

"The same rule applies where the breach is partial and not total; and to make good the warranty as to condition, the cost of repairs; and, as to freedom from liens, the cost of removing them, if that be the difference in actual value, between the article as warranted and the article as delivered, is all that can be properly recovered as damages, unless in exceptional cases of special damage. Whatever that difference, in the actual circumstances of the case, is shown to be, is the true rule and measure of damages. *Where the articles delivered are not what the contract calls for, as in the case of defective machines, the measure of the vendee's damages is what it would cost to supply the deficiency, without regard to the contract price. Benjamin v. Hillard*, 23 How. 149-167 (64 U. S. XVI, 518-522)."

In the case of *McCarthy v. Central Dredging Co.*, (C. C. A.) 203 Fed. 965, the respondent's scow was sunk and libelants made a contract to furnish a diver to assist respondent in raising the scow. Respondent intended to raise it by pumping, which

necessitated patching up the holes. Libelants' diver located a hole in the deck and attempted to patch it up, but failed to do so. On failing to raise the scow by pumping respondent then had her raised by jacks, and it was discovered that the hole had not been entirely covered by the diver. Respondent attempted to recover on a cross-libel the difference in cost. The court held, however, that respondent was entitled to recover only the amount which it would have cost, with perhaps some allowance for delay, to send another diver down to go over the work. That the respondent had no right after a few minutes pumping and no further investigation to abandon that method of raising the scow and hold the libelants responsible for the large expense of raising the vessel in a different way.

In *Southern Pacific Co. v. Fore River Shipbuilding Co.*, (C. C. A.) 219 Fed. 378, the action was to recover damages for an alleged breach of contract of guaranty as to the speed and coal consumption of a steamship which the defendant built for the plaintiff. It was held that plaintiff was entitled to recover under the proper rule of damages the cost of making the necessary changes in order that the vessel might comply with the contract and for the loss of the use of the vessel while they were being made.

*Walsh Construction Co. v. City of Cleveland*, 271 Fed. 701, on page 712:

“The measure of damages properly to be applied is that applicable to a contract which has



been substantially performed but into the performance of which has entered defective materials or faulty workmanship, or departures from the plans and specifications. In cases of this character, two rules have been applied, depending somewhat upon the circumstances of each case. One is that the contractor is entitled to recover the contract price diminished by the difference between the value of the building to the owner in its defective condition, and its value if perfectly constructed. This rule is applied whenever the structure or building is useful to the owner in its defective condition and it is neither fair nor reasonably practicable to remedy the defects by the making of repairs. In other cases where there is a failure to complete the work, and such failure may reasonably be remedied by the expenditure of additional labor and materials, *or where the defects are of such a character that they may be fairly and reasonably remedied by the expenditure of labor and materials*, the proper rule seems to be to deduct from the contract price such sums as would be reasonably necessary to complete the work according to the contract or to make such repairs. Sutherland on Damages, Par. 699; Stillwell Mfg. Co. v. Phelps, 130 U. S. 520, 9 Sup. Ct. 601, 32 L. Ed. 1035; Gleason v. Smith, 9 Cush. (Mass.) 484, 57 Am. Dec. 62; Pelatowski v. Black, 213 Mass. 428, 100 N. E. 831. No finding, as has been said, is made by the master as to the difference in value between the reservoir in its defective condition, and the contract price, nor how much less valuable the reservoir is to the owner by reason of faulty workmanship. No evidence seems to have been offered on this proposition. The burden of proof in that situation is apparently with the owner. Filbert v. Philadelphia, 181 Pa. 530, 547, 37 Atl. 545; District of Columbia v. Clephane, 110 U. S. 212, 3 Sup. Ct. 568, 28 L. Ed. 122."

*North Chicago St. Ry. Co. v. Burnham*, (C. C. A.) 102 Fed. 669, page 673:

“On any supposition, however, it is evident that the actual damage suffered by the plaintiff in error could not exceed the cost of making the changes of construction necessary to meet the requirements of the contract, and on that basis, therefore, the measure of recoupment should be determined. *Benjamin v. Hillard*, 23 How. 149, 167, 16 L. Ed. 518; *Railroad Co. v. Smith*, 21 Wall. 255, 22 L. Ed. 513; *Marsh v. McPherson*, 105 U. S. 709, 26 L. Ed. 1139; *Dushane v. Benedict*, 120 U. S. 630, 7 Sup. Ct. 696, 30 L. Ed. 810; *Manufacturing Co. v. Phelps*, 130 U. S. 520, 9 Sup. Ct. 601, 32 L. Ed. 1030; *Crouch v. Gutmann*, 134 N. Y. 45, 31 N. E. 271; *Keeler v. Herr*, 157 Ill. 57, 60, 41 N. E. 750.”

The important thing to notice in the foregoing cases is, that they establish that the damages implied by law in the present case would be the cost of sending a man down to the vessel at the Pacific Mail Company's pier to overhaul and make repairs to the clapper-valves in No. 2 hold, and for detention, if any, of the vessel during the time taken for such overhauling and repairs.

The damages for injury to cargo claimed in the present case are not implied by law, and they are, therefore, special damages. The Pacific Mail Company must, for that reason prove that at or prior to the consummation of the contract, the Bethlehem Corporation was notified by the Pacific Mail Company that, on completion of the repairs, it would load the vessel with certain cargo for a voyage to

cast coast ports, and it is immaterial that cargo vessels are generally used for such a purpose; that the Pacific Mail Company would rely upon the Bethlehem Corporation to make the vessel seaworthy for the voyage, at least as far as the work done by the latter was concerned, and that in event the Bethlehem Corporation failed to make the vessel seaworthy, to the extent indicated, it would be expected to pay for any damage to cargo caused by such a failure, and that the Bethlehem Corporation accepted such a liability as a condition of the contract. This, it will be recalled, is the rule in the early and leading English authority of *Hadley v. Baxendale*, but it is unnecessary to establish the rule by English authorities.

In the case of *Central Trust Co. v. Clark*, (C. C. A.) 92 Fed. 295, the court, in referring to general damages (that is, those implied by law as the necessary result of the breach), as damages implied by the contract itself, holds that other damages (special damages) can only be recovered when the liability therefor was assumed as a term of the contract.

“In the absence of proof aliunde of *knowledge by the defaulting party at the time the contract is made* of special circumstances which make other damages the natural and probable effect of a breach, such damages only as are implied by the contract itself, such as would naturally flow from its breach in the usual course of things, such as would reasonably be anticipated by the parties to such contracts *in the great multitude of such cases*, and such damages only, may be recovered. *Drug Co. v.*



Byrd, 93 Fed. 290; Railroad Co. v. Bucki, 16 C. C. A. 42, 46, 68 Fed. 864, 868 and 30 U. S. App. 454, 460; Hadley v. Baxendale, 9 Exch. 341, 354, 356; Primrose v. Telegraph Co., 154 U. S. 1, 29, 14 Sup. Ct. 1098; The Ceres, 19 C. C. A. 243, 72 Fed. 936, 943; Boyd v. Brown, 17 Pick. 453, 461; Ingledew v. Railroad, 7 Gray, 86, 91; Railway Co. v. Mudford Ark., 3 S. W. 814, 816; Kempner v. Cohn, 47 Ark. 519, 527, 1 S. W. 869."

In that case the seller failed to deliver a gear wheel and pinion to the buyer, a street railway company, within the time agreed. By reason of the delay the street railway company was unable to operate its cars for a certain period of time, and the delay necessitated a reduction of speed of its cars at other times. The seller was advised of these things after the making of the contract, and before the parts were delivered. The buyer sued for the damage caused thereby, but the court held that they could not be recovered because the seller had no knowledge of the special circumstances causing the damage at the time that the contract was made.

The case of *Central Trust Co. v. Clark*, *supra*, is also quoted with approval in *Lamon v. Speer Hardware Co.*, (C. C. A.) 198 Fed. 453, and *Northwestern Manufacturing Co. v. Great Lakes Engineering Works*, (C. C. A.) 181 Fed. 38.

In *Stebbins v. Selig*, (C. C. A.) 257 Fed. 231, the defendant breached an agreement to drill a well and install a pump for irrigation purposes upon the land of the plaintiff. By reason of such failure the

defendant's rice crop was damaged and he undertook to collect from plaintiff as damages the difference between the value of the rice actually raised, and that which would have been raised had it been irrigated. It was held that such damages were special and uncollectable in the absence of any provision in the contract indicating that such damages were contemplated by the parties. The court said:

*"One way of testing whether the defendant contemplated this consequence is to suppose that, had defendant been asked to agree to a clause in the contract that would make him liable in the way specified, would he have assented to the same? In our judgment there can be but one answer to this question: He would not. The foregoing principles of law are fully illustrated and sustained by the Supreme Court of the United States in Globe Refining Co. v. Landa Cotton Oil Co., supra, where the cases, English and American, are cited.*

This case in our opinion fully sustains the ruling of the trial court. While the complaint shows that the defendant was in the business of sinking wells for the irrigation of rice lands, *and knew that the plaintiff wanted the water to be pumped from the well in question to be used for the growing of rice*, there is no showing, in our opinion, that the plaintiff believed or contemplated, or that it was in the contemplation of either party, that if the defendant failed to perform the contract within 20 days he would be liable for the difference in value between the rice crop of the plaintiff and any rice crop raised upon any adjoining land."

In *Globe Refining Co. v. Landa Cotton Oil Co.*, 190 U. S. 540, 47 L. Ed. 1171, it was held that mere

notice to a seller of some interest *or probable action of the buyer* is not enough, necessarily as a matter of the law, to charge the seller with special damages on that account if he fails to deliver the goods. The court says, on pages 1173 and 1174, in quoting from the English case of *British Columbia Sawmill Co. v. Nettleship*, L. R. 3 C. P. 490, 500:

“I am disposed to take the narrow view that one of the two contracting parties ought not to be allowed to obtain an advantage which he has not paid for \* \* \*. If that (a liability for the full profits that might be made by machinery which the defendant was transporting, if the plaintiff's trade should prove successful and without a rival) had been presented to the mind of the ship owner at the time of making the contract, as the basis upon which he was contracting, *he would have at once have rejected it. And though he knew, from the shippers, the use they intended to make of the articles, it could not be contended that the mere fact of knowledge, without more, would be a reason for imposing upon him a greater degree of liability than would otherwise have been cast upon him.* To my mind, that leads to the inevitable conclusion that the mere fact of knowledge cannot increase the liability. The knowledge must be brought home to the party sought to be charged, under such circumstances that he must know that the person he contracts with reasonably believes that he accepts the contract with the special condition attached to it.” The last words are quoted and reaffirmed by the same judge in *Horne v. Midland R. Co.*, L. R. 7 C. P. 583; S. C., L. R. 8 C. P. 131. See also Benjamin, Sales, 6th Am. Ed. par. 872.”



These cases are not cited to establish the rule that, generally, loss of profits cannot be recovered as damages, but they are cited to the broad proposition that special damages cannot be recovered unless the circumstances show that the liability therefor was accepted by the defaulting party as a special condition of the contract.

The Pacific Mail Company claimed, and the District Court held, that the clause in the specifications (Apos. p. 18), "All work to be finished and vessel alongside Pier 44, or any other pier designated by owner, and ready to load cargo by 6:00 A. M. Oct. 11, 1923," operates to create such a special condition in the contract, for the repairs on the "Ecuador." It does not, even standing alone, but over and above that, this clause must be read and construed with other clauses in the documents evidencing the agreement.

In the advertisement for bids, to which the specifications were attached, are found the following clauses (Apos. pp. 15, 16):

"Repairs as specified are to be completed on or before 12:00 noon October 12, 1923, to the entire satisfaction of our Supt. Engineer or his representative."

"NOTE: In the award of contract no consideration will be given to possible earlier completion dates. All repairs that would interfere with loading of cargo must be finished and vessel available for loading berth not later than 8:00 A. M. Oct. 11, 1923."

Then follows the clause in the specifications quoted in the preceding paragraph.

The reasonable construction of these clauses is (1) that the vessel, with repairs considered as finished by the Bethlehem Corporation, should be delivered at the pier by 6:00 A. M. October 11, 1923; (2) that if directed by the Pacific Mail Company's Supt. Engineer, or his representative, to make additional repairs which would interfere with the loading of cargo, such repairs should be finished by 8:00 A. M. October 11, 1923; (3) that all other additional repairs, so directed, should be finished by 12 noon October 12, 1923. In any event, no reasonable construction could raise out of the language of these clauses an agreement by the Bethlehem Corporation to pay for damage to any cargo which might be injured in event that it breached its agreement.

In the present case there are no circumstances which tend to show that at the time the contract for repairs was made, the Pacific Mail Company even intimated to the Bethlehem Corporation that it would hold the latter liable for damage caused to cargo, and so, of course, it cannot possibly be inferred that the Bethlehem Corporation accepted such a liability as a condition of the contract.

## **2. The Special Damage Rule Applies to a Liability Arising Out of a Collateral Contract.**

The answer of the Pacific Mail Company to the libel on file alleges as an affirmative defense, and

the bill of lading shows, that the contract under which the cargo was shipped provided that the Pacific Mail Company should only be required to exercise due diligence to make the vessel seaworthy at the time of shipment, commencement of the voyage or on the voyage, and that if such due diligence had been used neither the vessel nor the Pacific Mail Company should be held responsible for, among other things, unseaworthiness. (Apos. p. 11; Libellant's Exh. No. 5.)

Under the contract, then, there was no liability on the Pacific Mail Company's part to the shippers from the mere fact itself that the vessel was unseaworthy by reason of the defective condition of the clapper-valves, or in any other respect. But such liability does arise by reason of the failure of the Pacific Mail Company to exercise due diligence to make the vessel seaworthy at the commencement of the voyage, as provided in the contract between the Pacific Mail Company and the shippers.

*Braker v. Jarvis Co.*, 166 Fed. 987;

*Sanbern v. Wright Lighterage Co.*, 171 Fed. 449;

*Martin v. The Southwark*, 191 U. S. 1, 48 L. Ed. 65;

*The Willdomino*, (C. C. A.) 300 Fed. 5.

The admitted insufficiency of the inspection made by the officers of the "Ecuador", clearly establishes a breach of the contracts by the Pacific Mail Company with its shippers to exercise due diligence to



make the vessel seaworthy at the commencement of the voyage in question and its consequent liability to the shippers.

Now if the Pacific Mail Company had employed the Bethlehem Corporation to discharge the obligation of the Pacific Mail Company, under its contracts with the shippers, to exercise due diligence in making the vessel seaworthy by a proper inspection at the commencement of the voyage in question, a different case would be presented. No such allegation is made, however, in the answer of the Pacific Mail Company to the libel or in its petition to have the Bethlehem Corporation brought in as a third party. The answer alleges that in the exercise of due diligence the Pacific Mail Company contracted with the Bethlehem Corporation for the repair and overhauling of the vessel, and in particular for the overhauling and repair of all clapper-valves, and that, relying upon the agreement by the Bethlehem Corporation to put the vessel in a seaworthy condition and fit to receive cargo, it loaded and stowed cargo on the vessel. (Apos. pp. 11 and 12.) The petition alleges that the Pacific Mail Company, relying upon the performance of the contract in a workmanlike manner, and to return the vessel ready to receive cargo, and without any knowledge of the breach, stowed the cargo in No. 2 hold. (Apos. p. 22.) The allegation in reference to the vessel being returned ready to receive cargo has been disposed of in the preceding section.

These allegations in the Pacific Mail Company's answer and petition raise the question of whether, in a case where a defendant breached a contract between it and plaintiff, and it further appears that plaintiff, in relying upon defendant's performance, was induced not to perform obligations of a contract between plaintiff and a third party, is the defendant liable for damages incurred by plaintiff on the breach on such a collateral contract. This question involves an application of the rule established in the preceding section concerning the notice of damages which are not implied by law as necessarily flowing from a breach, only here such special damages arise from another contract. The principle is precisely the same, however, as the collateral contract is merely an illustration of one of the special circumstances causing damage, and under which it follows that the defendant must have had such notice as would imply that plaintiff's liability upon the collateral contract was accepted as a condition of the contract between plaintiff and defendant.

The answer to the question above propounded is, therefore, quite obvious, but, regardless of whether the question is framed as above or assumed that the Pacific Mail Company relied upon the performance of the repair contract by the Bethlehem Corporation for the performance of an obligation in a contract of affreightment between the Pacific Mail Company and a shipper, still there would be no liability on the Bethlehem Corporation for damages suffered by

the Pacific Mail Company through its breach of the latter contract, unless the Bethlehem Corporation had notice, of the kind heretofore described, of that affreightment contract at the time that it entered into the agreement with the Pacific Mail Company for the repair of the vessel.

In the following cases the special damage rule was applied to damages suffered on collateral contracts and they cannot be distinguished on the ground that the damages claimed were lost profits. Such a loss is merely one of the various kinds of special damages and they are all governed by the same rule.

*Halloway v. White Company*, (C. C. A.) 151 Fed. 216;

*Tompkins Co. v. Monticello Co.*, 153 Fed. 817;

*Pusey & Jones Co. v. Combined Locks Paper Co.*, 255 Fed. 700, affirmed 258 Fed. 989;

*Mitsubishi Shoko Kaisha v. Davis*, 291 Fed. 882.

As pointed out in those cases the mere fact that the Bethlehem Corporation presumably knew that the Pacific Mail Company would enter into contracts with third parties for the transportation of cargo, and that it might be damaged by the failure to replace a bonnet on a clapper-valve, is insufficient to infer that the Bethlehem Corporation agreed to assume the liability for that damage; that such a liability involves matters within the exclusive control of the Pacific Mail Company subse-



quent to the execution of the repair contract, such as the fixing of values on cargoes, the class of cargoes to be carried and the extent of the Pacific Mail Company's liability under the contract of carriage.

In the case of *Pusey Jones & Co. v. Combined Locks Paper Company (supra)*, 255 Fed. 700, affirmed 258 Fed. 989, the same general ruling was made, that is:

“unless special circumstances are shown with respect to which the parties must be deemed to have contracted.”

It appears in that case that the plaintiff had purchased of the defendant a paper making machine, and defendant was to install it at a certain time. The plaintiff then entered into contracts with third parties for the sale of paper to be manufactured by the machines to be furnished by the defendant, but in the contracts with the third parties plaintiff reserved the right to begin delivery at a date later than the actual installation of the machines. As the court observed, the contracts were made contingent in their commencement upon the very circumstance of delay, which was the foundation of the action against the defendant. Under those circumstances it was held that any damages on these collateral contracts could not have been contemplated by the parties at the time that the agreement was made between plaintiff and defendant:

“As I understand the rule, the contemplation of one of the parties is not sufficient; it must

be a mutual and reciprocal contemplation produced by such particularity of attendant circumstances as should preclude both parties from saying that they were not, in effect, in law incorporated into the engagement."

So in the present case the contract between the Pacific Mail Company and the shipper expressly contemplated that the vessel might be unseaworthy after the repairs were made and it was provided in the contract between them that any damage resulting from unseaworthiness should not be charged against the Pacific Mail Company, provided that the latter company performed a duty to the shipper, which, under the law, it was bound to perform anyway, in seeing that the vessel was seaworthy at the commencement of the voyage.

Moreover it affirmatively appears from the evidence that the failure of the Pacific Mail Company to exercise due diligence in inspecting the vessel prior to the voyage was not due to its reliance upon the contract with the Bethlehem Corporation to repair the clapper-valves.

The District Court found (Apos. p. 791):

"It is true that it was part of the ordinary duty of the chief engineer of the vessel before cargo was received aboard to inspect, among other things, the clapper-valves. On this occasion relying, as he had a right to do, upon the performance of its contract by the shipbuilding corporation, he made no such examination."

We take it to be a matter of common knowledge that it is the duty of the first officer of the vessel to

inspect the holds of the vessel, including the clapper-valves located therein, to ascertain if they are in a fit condition to receive the intended cargo, and Chief Engineer Murray of the "Ecuador" so testified (Apos. pp. 771, 772):

"Q. That is in your department, of course, isn't it Mr. Murray—the clapper-valves belong to your department?

A. No, sir.

Q. Not under the supervision of the engineer?

A. Only those that are in the engine-room department, that is, in the fire-room, bunkers and over the fuel tanks.

Q. And you have nothing to do with those in Nos. 1, 2, 3, 4 or 5?

A. Not directly, no, sir; those are cargo holds under the jurisdiction of the deck officers."

Of course, if it were found that any temporary repairs were needed on the mechanical parts of the clapper-valves, it would be accomplished by the engine room department.

First Officer Dowdy of the "Ecuador" testified he had never seen Mr. Murray in the cargo holds of the "Ecuador" except on occasions when the representative of the insurance company and the shipping bureau made their inspections. (Apos. p. 283.)

First Officer Dowdy, whose duty it was as a representative of the Pacific Mail Company to inspect the vessel, gave as an excuse for his negligent inspection that he relied upon the Bethlehem Corporation to put the clapper-valves in a proper con-



dition, and the same allegation is made in the Pacific Mail Company's petition. There was a total failure of proof of any such claim or allegation, however, as the first officer admitted that he had no knowledge of whether the Bethlehem Corporation agreed to repair the clapper-valves. (Apos. pp. 284, 285, 286.)

“Q. Did you see the tender or repairs that were to be made on the ‘Ecuador’ before the bids were asked for?

A. No, sir, I don't get any of those papers, whatsoever. I get my own report list, which is turned in, and I keep a copy for myself, and whatever is erased from there I don't know. All I know is that Mr. Montcaster tells me, ‘You can't have this, you can't have that, you will get this, you will get that.’ That is all I have.

Q. On your list there was nothing said about repairs to the clapper-valves?

A. No, sir.

(Stipulated that objection might be deemed to be interposed to this line of examination.)

Mr. LILLICK. Q. There was nothing on your requisition to Mr. Montcaster or to the company having to do with clapper-valves, was there?

A. Nothing whatsoever.

Q. Did you see the request or demand to the office that Mr. Murray made?

A. No, sir, I have nothing to do with that.

Q. You didn't know whether the contract provided for repairs to clapper-valves, or not, did you?

A. No, sir, I did not.

Q. You knew nothing about that at all, did you?

A. I didn't know anything at all about that.

Q. Then you did not even know that the clapper-valves were to be repaired, did you?

A. I did not.

Q. You never saw the contract that was entered into between the Bethlehem Shipbuilding Company and the Pacific Mail Steamship Company, did you?

A. No, sir."

This testimony not only fails to establish the allegation that the Pacific Mail Company relied upon the performance of the repair contract by the Bethlehem Corporation for the performance of an obligation under its contract with the shipper, or induced it not to perform such an obligation, but on the contrary affirmatively shows that the representative of the Pacific Mail Company, whose duty it was to perform that obligation, did not rely upon the repair contract with the Bethlehem Corporation. Even if he had, as previously shown, the damages resulting from an affreightment contract cannot be collected from the Bethlehem Corporation.

Lastly, it should be borne in mind that the liability, if any, of the Bethlehem Corporation is not enlarged by the fact that it is brought into this action as a third party respondent and compelled to answer the libel of the shipper. Its liability in this action is measured by its contract with the Pacific Mail Company precisely the same as if the Bethlehem Corporation and the Pacific Mail Company were the only parties to the action. (*The Lysefjord*, 262 Fed. 623.)

### 3. The Authorities Cited by the District Court Do Not Support Its Conclusions of Law.

After finding that the breach of the repair contract was the efficient cause of the damage the District Court ruled in its opinion (Apos. p. 790):

“Cases supporting the view that the third party respondent is liable for the amount which the steamship company may be compelled to pay to the libellant in compensation for the damage sustained by it are: *Ellerman Lines v. Smith Drydock Co.*, 18 Lloyds’ List L. Rep. 172; *The Louis Luckenbach*, 207 Fed. 66; *Pan-American Pet. Co. v. Robins Drydock Co.*, 281 Fed. 97; *Mowbray v. Merriweather*, 2 Q. B. 640; *Boston Woven Hose & Rubber Co. v. Kendall*, 178 Mass. 232; 59 N. E. 657.”

These cases are also cited to the point that the Pacific Mail Company owed no duty of inspection to the Bethlehem Corporation, and so we will consider both of those points in the discussion of the cases cited by the District Court.

Before proceeding any further, we wish to disclaim any attempt to argue that ordinarily the Pacific Mail Company owed any general duty to the Bethlehem Corporation to inspect the repairs on the vessel after they were finished, or to inspect the holds to ascertain if they were in a fit condition to receive the cargo or to take any soundings on the voyage.

In its opening brief in the trial court the Pacific Mail Company took the position that the Bethlehem Corporation had breached its contract and without



attempting to show that the damages claimed were such as might be collected in this action, argued that if the Bethlehem Corporation defended on the grounds that the damage was caused by the Pacific Mail Company's breach of duty to its shipper in failing to inspect the holds of the vessel or to take soundings, such defenses would be invalid under the active and passive negligence rule.

Our answering brief freely admitted the general rule, namely:

“That where a defendant is guilty of a positive act of negligence and the plaintiff, if guilty only of a technical or constructive negligence, is held liable to third parties for damages directly and proximately resulting from that act, the plaintiff is entitled to be indemnified by the defendant”

as applied to cases involving breaches of duties imposed by law. Although it is clearly inapplicable to a suit for the breach of a contract, still the rule does establish that the Pacific Mail Company owed no legal duty to the Bethlehem Corporation, independently of a stipulation therefor in the contract, to inspect repairs when made, or to take soundings. But even in purely tort actions the rule would not be applied where prior to the injury the plaintiff has knowledge of facts which put him upon notice that a defect in the article furnished by the defendant would cause further damage, if used in its defective state.

Notwithstanding that the Pacific Mail Company again made as its principal point in its reply brief,

that under the rules stated the Pacific Mail Company owed no duty of inspection to the Bethlehem Corporation. That this mislead the trial court fully appears in the following excerpts from the opinion (Apos. p. 791, 793, 794):

“While the steamship company was required in the operation of its vessel to exercise care and diligence to protect the shipper from loss, it owed no such duty to the shipbuilding corporation.

\* \* \* \* \*

“As above stated, even if there were negligence here it would be at most a breach of duty to the shipper and not to the repairer of the vessel. It has been held in a similar case, where the ship owner sought to recover from the repairer the sum it had been compelled to pay on account of damage by seawater by reason of defective repairs, that the owner owed no duty to the ship’s repairer to take any soundings whatever.”

The court then discussed the trial court’s ruling made in the English case of *Ellerman Lines v. Smith Drydock Co.* (*supra*) on the defense there made that the damage to the cargo was due to the negligence of the Steamship Company in not making proper soundings.

In order to prevent the possibility of such a false issue from again forming the principal basis of the decision in this action, we repeat that the Pacific Mail Company owed no duty of inspection, or to take other precautions until it had knowledge of facts sufficient to put it upon notice that water

in large quantities might enter, or was entering, through the clapper-valve in No. 2 hold.

The District Court, however, was so thoroughly saturated with the rule that there was no duty of inspection owed to the Bethlehem Corporation, by the frequency of its repetition in the Pacific Mail Company's brief, that in order to make the rule apparently bear on an issue in the case, it was compelled to hold that the Bethlehem Corporation's claim, stated in the preceding paragraph, was equivalent to no more than a claim that the Pacific Mail Company was guilty of negligence in not discovering the unsecured bonnet on the clapper-valve in question (Apos. p. 790). Then follows the above quoted statements by the court in regard to the duty of inspection not owed to the Bethlehem Corporation.

We think that it will be admitted without argument, that a general duty of precaution is one thing, and a duty of precaution in the light of particular circumstances and knowledge of certain facts, is entirely a different thing. But let us consider the cases cited by the court on this point, and also on the proper rule of damage in actions *ex contractu*.

In *Ellerman Lines v. Smith Drydock Co.*, 18 Lloyd's List L. Rep. 172, (not an appellate court decision) the action was brought by the Steamship Company for defendant's breach of contract in failing to repair the drain valve on a vessel and



the damage claimed was for injury to a shipper's cargo, which the Steamship Company had been compelled to pay the shipper. The court found that the defendant did not agree to repair the valve, and so judgment was given for the defendant.

The law established by that case is that where a defendant did not agree to repair a drain pipe on a vessel it cannot be held liable for damage to cargo caused by the drain pipe being in an unrepaired condition.

To argue conversely from this ruling that if a repairer does agree to repair a drain pipe, but fails to do so, he will be liable for all damage caused thereby which the vessel's owner may be compelled to pay third parties, would be on the face of it most erroneous, illogical and fallacious. Yet that was the argument of the Pacific Mail Company in its brief to the lower court where it set out a full report of that case. If the argument is good, then in a case where a plaintiff sues on an alleged contract, for the breach of which he claims extremely speculative damages, and the court found that defendant did not enter into such an agreement, and gave judgment for the defendant, the law of that case would be that if the defendant had made such an agreement he would be liable for the extremely speculative damages caused by its breach. Absurd, of course, but that was the Pacific Mail Company's argument to the trial court on the law of the above case.

True, the court in that case says that if the facts had been different, it might have held otherwise; to which statement we should add by fair inference "provided that the damages claimed were such as are allowable under the law on contracts and special circumstances as they might appear from the evidence, if the question of damage had been an issue."

The question of the proper rule of damages for breach of contract was never raised or discussed in that case, nor was it necessary. Also the court correctly, though unnecessarily said, that the Steamship Company owed no duty to the defendant under the circumstances to take soundings, but if there had been any evidence showing that the vessel's officers had knowledge of facts sufficient to put them upon notice of the defective drain pipe, the court probably would not have made that statement.

In the *Louis Luckenbach*, 207 Fed. 66, a stevedore was injured by a breaking of a strongback on a vessel and he brought an action in tort against the charterer and the owner. Both of those parties made separate settlements with the stevedore and thereafter the charterer brought an action against the owner, not for a breach of the charter party, but, as appears from the decision of the lower court, 203 Fed. 706, on page 708, for the owner's negligence in failing to keep the strongback in a safe condition. The owner was held liable. If, however, the charterer had brought an action for a breach of the contract, as set out in the charter

party, by reason of the owner's failure to keep the strongback in a proper condition as therein provided, regardless of whether he negligently failed to do so or not, and alleged as damage that it caused a breach of the charterer's contract with the stevedore, regardless of any violations of the charterer's legal duty to the stevedore, the court would then have had occasion to pass on the rule of damage in contract actions.

Although the condition of the strongback could have been discovered by the exercise of due diligence, it did not appear that the charterer had any knowledge of facts which would lead it to believe that the strongback might have been defective, and so, of course, the charterer owed no duty of inspection to the owner.

The opinion in that case cites *Mowbray v. Merriweather* and *Boston Woven Hose & Rubber Co. v. Kendall*, cited in the District Court's opinion in the present case, but the same distinctions exist in those cases. Beyond a doubt if a defendant manufacturer negligently delivers a defective article to be used by the plaintiff's workman and the workman is injured, the defendant manufacturer would be liable to the workman. If the workman collected the damages from the plaintiff by reason of the relation between them of master and servant, the plaintiff will be entitled to indemnity from the defendant manufacturer, if he had no reason to believe that the defect existed. This, however, is no authority for any rule on damages arising out



of a breach of contract, and regardless of the violation of any duty imposed by law. Even if the above English and Massachusetts cases purport to hold that such a ruling should be made in an action *ex contractu*, it would be contrary to the very great weight of authority on the proper rules of damage in such an action, as heretofore pointed out.

In *Pan-American Pet. Co. v. Robins Dry Dock Co.*, 281 Fed. 97, the action was brought by the Steamship Company for the breach of a contract to repair a vessel, in that, the telegraph apparatus from the bridge to the engine-room was not repaired as agreed by the defendant. That case, however, did not involve a liability on a shipper's contract for the transportation of cargo, but the damages claimed arose out of a collision for which the vessel repaired was held liable. The trial court found that the respondent repairer was not guilty of negligence and dismissed the libel. The Circuit Court of Appeals held that the question of negligence was not material (p. 108) because the suit was brought on contract and then laid down the rule that where the owner of the vessel proved a breach of the contract to repair the vessel, thus establishing a *prima facie* case, the weight of the evidence then shifted to the repairer to prove that he had fully performed the contract. That burden was not met by the respondent repairer. The lower court held that the burden was on the libellant, vessel owner, to prove negligence on the part of the defendant, and so the judgment of the lower court

was reversed. The question of damages was not discussed in the lower court, nor could it even have been raised, because the judgment was for the respondent.

We do not understand that there was any evidence of damage given in the Appellate Court, and so the question as to the proper rule of damage for breach of contract could not have been raised in that court. Beyond a doubt the respondent will be held liable on a retrial of the case for general damages for his breach, the cost of putting the telegraph in the condition specified in the contract, but whether or not the libelant will be able to collect any special damages claimed, remains to be seen. If he does the evidence will have to show that the repairer accepted the liability for those special damages as a condition of the contract. It is no answer to say that if the case is referred to a commissioner he will be called upon only to ascertain the amount of damages. In ascertaining that amount the commissioner will necessarily be called upon to say what items of damage claimed are proper and what items are improper. But whether the question of the proper rule of damage in contract actions is raised in a retrial of that case is not material, as the failure to raise it would not be authority for the contention that therefore the Bethlehem Corporation ought not to raise that question in this case.

There was no evidence in the above case showing that the libelant had knowledge of any facts suffi-

cient to put it upon notice of the defective telegraph. Furthermore, it was found by the court that even if the usual test had been made, it would not have disclosed the defect.

If, in the words of the Circuit Court of Appeals in *Central Trust Co. v. Clark (supra)*, in the great multitude of cases involving the failure to make repairs on a vessel according to contract, the necessary result of such a breach has been injury to a shipper's cargo, it is remarkably strange that no such cases ever got into the courts. We have made a diligent search for such a case in the American Courts regardless of whether the action was brought in contract or in tort, but we have not been able to find any, nor have the proctors for the Pacific Mail Company. A search of the English authorities reveals only one case where such a claim was made, and in that case the judgment was given for the defendant. We may then safely assert that there is no authority for the Pacific Mail Company's contention that it may collect as general damage for the breach of the contract, damages to a shipper's cargo. There is no authority holding that such damages may be collected as special damages because the Bethlehem Corporation knew that the vessel, when repaired, would be used to carry cargo, and hence accepted that liability as a condition of the repair contract. There is no authority holding that the Pacific Mail Company owed no duty to the Bethlehem Corporation to take proper precautions by inspection, soundings, or other



means after it had knowledge of facts sufficient to put it upon notice that water in large quantities might enter, or was entering, through the clapper-valve in No. 2 hold. This brings us to the question of whether the Pacific Mail Company had knowledge of such facts, which is discussed in the following section:

**4. The Damages Claimed Were Caused by the Pacific Mail Company's Failure to Prevent Further Loss.**

Independently of the foregoing reasons why the Pacific Mail Company should not be permitted to compel the Bethlehem Corporation to pay for the breach of the Pacific Mail Company's obligations to its shippers, there can be no liability on the Bethlehem Corporation for that part of the damage which the Pacific Mail Company might have prevented by the exercise of reasonable diligence.

When the "Ecuador" was redelivered to the Pacific Mail Company, on the morning of October 11, 1923, the Bethlehem Corporation had breached its contract in failing to repair the clapper-valves in No. 2 hold. The Bethlehem Corporation then and there became liable for the cost of completing the repairs in that hold in order to make the job comply with the specifications of the contract. This would amount to about one hour's work in fixing the valves, and perhaps a delay for that length of time in loading cargo into the hold. No such damages are claimed, however. Instead the Pacific Mail Company seeks to fasten upon the Bethlehem Corporation a liability for damages to cargo which

occurred some three days after the vessel had been in the exclusive possession of the Pacific Mail Company.

In the case of *Warren v. Stoddart*, 105 U. S. 224, 26 L. Ed. 1117, on page 1120, the Supreme Court said:

“The rule is, that where a party is entitled to the benefit of a contract and can save himself from a loss arising from a breach of it at a trifling expense or with reasonable exertions, it is his duty to do it, and he can charge the delinquent with such damages only as with reasonable endeavors and expense he could not prevent. *Wicker v. Hoppock*, 6 Wall., 94 (73 U. S., XVIII., 752); *Miller v. Mariner’s Church*, 7 Greenl. (Me.), 56; *Russel v. Butterfield*, 21 Wend., 304; *Ketchell v. Burns*, 24 Wend., 457; *U. S. v. Burnham*, 1 Mason, 57; *Taylor v. Read*, 4 Paige, 571.”

The District Court correctly ruled (Apos. p. 790):

“It is a familiar principle of law that where one is responsible to another in damages for the breach of an obligation it is the duty of the latter, upon discovering the impending damages, to use ordinary care and prudence to minimize the consequence of the other’s breach of contract. (*Ash v. Loo Sing Lung*, 177 Cal. 356, 362; 17 Corp. Jur. 770.)”

Then follows the erroneous ruling that because the Pacific Mail Company ordinarily owed no duty to the Bethlehem Corporation to inspect the vessel, or to take soundings; therefore, if inspections were made and soundings were taken nevertheless, and knowledge of certain facts were gained thereby, still

the Pacific Mail Company would owe no duty to the Bethlehem Corporation to take proper precautions against further damage, apparently for the reason that such knowledge was gained through inspections and soundings which the Pacific Mail Company was not required to make, as far as the Bethlehem Corporation is concerned. The unsoundness of this reasoning has already been discussed.

But, says the District Court (Apos. p. 791):

“Conceding for argument’s sake that the position of the third party respondent in this behalf is sound, still it does not appear from a fair and impartial review of the evidence that the steamship company was guilty of any negligence.”

We assume that the District Court did not mean to rule that actual knowledge of the impending damage by the Pacific Mail Company was necessary before any duty arose to prevent that damage. If actual knowledge is essential, a plaintiff could merely testify that he closed his eyes to what he might have observed otherwise, and thus the familiar principle of law stated by the District Court would be completely nullified in so far as its practical application is concerned. In no case would a plaintiff ever admit that he actually knew the impending damage which could have been prevented, would occur. If he was willing to make such an admission he never would have brought the action, and attempt to collect the amount of that damage. In every case where the rule to minimize



damages has been involved, the court has been compelled to say whether, under the circumstances, the plaintiff ought to have known of the impending damage. If it is found that he ought to have known of such damage, this would be held equivalent to actual knowledge, and it would certainly follow that the plaintiff was guilty of negligence in not taking proper precautions to prevent the threatened damage. Thus, the issue on this branch of the case is squarely presented, namely, whether the officers of the "Ecuador" ought to have known that the cargo in No. 2 hold would be injured by sea water flowing into that hold through the clapper-valve. If they had knowledge of facts which indicated that water would, or was, flowing into that hold, it will no doubt be admitted that it was their duty to prevent damage to the cargo by keeping the hold pumped out, which the pumps were fully capable of doing.

After the "Ecuador" was delivered to the Pacific Mail Company at Pier 44, San Francisco, on the morning of October 11, 1923, the Government officials fumigated her. First Officer Dowdy then inspected the vessel to see if she was seaworthy in all respects for the voyage, and the cargo to be carried. Captain Boyce of the "Ecuador" testified that all of the vessel's officers went into No. 2 hold prior to the loading and that it was their duty to do so. (Apos. p. 250.) By this inspection the Pacific Mail Company owed to its shippers the duty of discovering every defect in that hold which would make the vessel unseaworthy, and which was not

a latent defect. Captain Boyce admitted that the defects in the clapper-valves were patent and not latent defects. (Apos. pp. 253, 254.)

Now after the injury occurs, it is a perfectly simple matter for Dowdy to take the stand and testify that he looked only at the floor boards on the occasion in question. But what he may say now is not very material, because the essential point is that he was down in the 'tween-deck of No. 2 hold prior to the time that any cargo was placed therein, and he could have seen that the bonnets were not fastened on the clapper-valves if he had looked. Even the stevedores, who owed no duty to anyone to inspect the vessel, saw daylight through the ship's sides through the forward port clapper-valve in No. 2 hold. (Pacific Mail Company's witnesses Holsten, Apos. p. 114; Trumure Apos. p. 125; Lawson, Apos. p. 133; Kalnin, Apos. p. 153.) Hence it may be said with the greatest reason that he ought to have known of their defective condition, and because he now says that he chose to close his eyes to any possible defects in the clapper-valves will not justify a ruling that therefore he ought not to have known of their condition. Over and above that the court is entitled to take into consideration that one of the very purposes of his inspecting the hold was to see that no defects existed in any of the appliances in that hold, including these clapper-valves, and it is not at all material that he owed that duty to the shipper instead of the Bethlehem Corporation. That would

in no way establish that he did not inspect the hold or alter his purpose in making the inspection.

But the foregoing is not the only reason why it should be held that Dowdy ought to have known of the defective clapper-valves in No. 2 hold. One of the stevedore foremen called his attention to the fact that daylight could be seen through the ship's side in No. 2 hold. He went into that hold with the foreman, who pointed out the place, and found that the bonnet was off the forward port clapper-valve. Dowdy then called the chief engineer, Murray (Apos. p. 259), and the chief engineer fixed the valve in about 15 minutes. (Holsten, Apos. p. 115.) This would have suggested to an ordinarily prudent man that possibly the other valves in No. 2 hold had been left open, and it did to First Officer Dowdy.

(Apos. p. 261):

“Q. After the chief engineer had set up the bolts on this bonnet, as you have described, what next did he and you do?

A. We went by to locate the other clapper-valves which were located in No. 2, and find out if all those clapper-valves were set up; we did the best we could do, we went on top of the cargo, which gives just enough space to wiggle through between the frames, and with a flash light we looked down where the cargo cannot be stowed, a space of a little more than a foot—

Q. Just let me stop you for a second; did I understand you to say there was enough space to wiggle through?

A. Yes.

Q. You say you wiggled through to look at the other clapper-valves in No. 2?



A. Yes.

Q. Which were those?

A. The after one on the port side in No. 2 and the others on the starboard side of No. 2 also."

Chief Engineer Murray also testified that he crawled over the cargo to inspect the clapper-valves located on the port and starboard sides aft in No. 2 hold, but that he was unable to see them on account of the cargo. (Apos. p. 42.) It is a significant circumstance that while both Dowdy (Apos. p. 262) and Murray (Apos. p. 422) testified that they went into other holds of the vessel and looked at the clapper-valves not covered with cargo, they made no such efforts to examine the ones which were covered as were made to examine those covered in No. 2 hold.

The fact that the cargo obscured the view of the other valves in No. 2 hold, in no way prevented Dowdy or any one delegated by him, from stepping to the telephone on the dock and inquiring of the Bethlehem Corporation whether or not the bonnets on the other clapper-valves in No. 2 hold had been put in place. If that had been done, as it should have been, it would have been the work of a very few minutes for the Bethlehem Corporation to make inquiry and then send a man down to the vessel to repair the other two valves.

The condition of the clapper-valve forward on the port side in No. 2 hold was discovered about 3 P. M. on Friday, October 12, 1923. (Pacific Mail

Company's witness Trumure, Apos. p. 127.) This valve is located about 6 feet above the floor of the 'tween-deck, and so is the one aft on the port side. The starboard clapper-valve is about 30 inches above the floor of the 'tween-deck. The 'tween-deck is 8 or 9 feet in height. (Pacific Mail Company's witness Trumure, Apos. p. 130.) At that time there were two carloads of copper on the floor of the 'tween-deck aft, piled from two to two and one-half feet high. (Pacific Mail Company's witnesses Triton (Apos. p. 74); Lawson (Apos. p. 137); Trumure (Apos. p. 128).) The placing of the cargo then in the 'tween-deck is described by the Pacific Mail Company's witnesses as follows:

HOLSTEN (Apos. p. 110):

"Q. At that time what was the condition as to the stage in loading which had been reached in No. 2 'tween-deck?

A. All the after end was full and both wings were full, all but about eight or ten feet abreast the hatch.

Q. How about the forward end up where you saw this light and where the work was done?

A. In the forward end there was a space there of about 12 feet where they had not finished yet."

TRUMURE (Apos. pp. 127, 128):

"Q. What state had the loading reached at that time, in the after part of No. 2 'tween-deck?

A. It was approximately loaded full, within four or five feet up to the place where the clapper-valve was, from either side, from the forward end and the after end.

Q. Which clapper-valve are you referring to?

A. That was on the port side, forward.

Q. The one where you saw this work done?

A. Yes, where this work was done."

CHRISTIAN (Apos. pp. 159, 160):

"Q. What portion of the 'tween-deck hold had cargo in it when these men were working on the pipe?

A. The after part of the 'tween-deck.

Q. How far forward—up to the hatch?

A. Right up to the hatch."

DOWDY (Apos. pp. 298, 299):

"Q. And you say that the square of the hatch was filled up with cargo?

A. No, the square of the hatch was not filled up, neither was the front of the forward bulk-head filled, but built around the square of the hatch was all filled up.

Q. Aren't you mistaken about that, Mr. Dowdy, because you reached the port clapper-valve in the forward portion, and there was no cargo there; there was no cargo there, was there?

A. No, not at that time.

Q. How far back of that was the space unfilled with cargo?

A. From about one-third of the hatchway forward.

Q. What was in there, flour?

A. There was general merchandise—flour, boxes, gunny bags, beans."

MURRAY (Apos. p. 420):

"Q. What was the condition in the after part of the 'tween-deck as to cargo?

A. It was loaded up full with cargo.

Q. How wide was the spread of the cargo? Do I make myself clear talking in non-sailor



language? By the 'spread' I mean the width; from side to side athwartships.

A. Athwartships there was a space clear in the middle from the hatches for the cargo to land, and they were lifting the cargo from that space to the wings."

From this testimony of the Pacific Mail Company's witnesses we may fairly conclude that at 3 P. M. on Friday, October 12, 1923, when the defective clapper-valve was discovered in No. 2 'tween-deck, the after end was loaded with copper, at least two feet high. Now if, as testified, the height of the 'tween-deck was about nine feet, and allowing, say a two-foot space between the top of the cargo and the ceiling, through which Murray and Dowdy crawled, this would make the general cargo in the aft end some five feet high from the top of the copper. The narrow spaces between the sides of the 'tween-deck and the hatch coaming were filled, except about ten or twelve feet on each side, which was used for loading. There was no cargo in the square of the hatch or in the forepart of the 'tween-deck. The square of the large hatch filled to the ceiling of the 'tween-deck certainly would hold more cargo than the small amount then stowed along the sides of the hatch, and so it is a fair statement to say that the 'tween-deck was considerably less than one-half full.

Now the question arises: suspecting, as First Officer Dowdy did, and as he could have been advised within a short time, that the bonnets were not on the clapper-valves located aft in No. 2 hold, how

long would it have taken to have removed a sufficient amount of cargo in order to repair those valves? Dowdy testified that all of the cargo would have to be taken out of the 'tween-deck in order to get at those valves, and that it would take several hours. (Apos. p. 299.) When pressed for a statement as to the number of hours, the highest estimate he dared to give was six hours. (Apos. p. 300.) It appears, however, that after the forward port clapper-valve was fixed the balance of the 'tween-deck was filled at 5 P. M. on Friday (about two hours), except the space in the wings of about six or eight feet, and it would have taken about 20 minutes to have filled that. (Pacific Mail Company's witness Triton, Apos. p. 70.) In fact, that space and the trunkway of the hatch, that is, the square of the hatch, were filled in two hours, making a total of about four hours to completely load more than half of the 'tween-deck. (Triton, Apos. pp. 76 and 77.)

If, as it appears, more than half of the cargo of the 'tween-deck could be, and was, loaded in about four hours, it certainly would not have taken any longer a time than that to have unloaded all of the cargo in the aft end of the 'tween-deck. But it was unnecessary to take out all of the cargo loaded there in order to get at the clapper-valves. It was unnecessary to remove the two carloads of copper, as they did not come up above the starboard clapper-valve aft, which was the lower of the two valves; being about 30 inches above the floor of the 'tween-deck. It was unnecessary to take out all of the

general cargo loaded on top of the copper in order to get at the port clapper-valve aft in the 'tween-deck, because that valve could not have been more than a foot or two below the top of the general cargo; it being some six feet above the floor of the 'tween-deck, and the general cargo on top of the copper could not have been higher than seven feet above the floor. As for the starboard clapper-valve aft, a small channel or alley way could have been made through the general cargo in a very little time, especially in view of the fact that there were open spaces in the 'tween-deck alongside of the square of the hatch and in the forward end to which this cargo could have been shifted. All of this undoubtedly could have been accomplished in about two hours. But let us make a liberal allowance and increase this calculation 100% by estimating that it would have taken four hours to have shifted a sufficient amount of cargo in order to fix the other two valves in No. 2 hold.

The correctness of this estimate is further supported by the time that it took to unload the cargo at Wilmington, not only in the 'tween-deck, but including the square of the hatch from the shelter deck to the main deck. The "Ecuador" arrived at the dock in Wilmington about 10 A. M. or after, Monday, October 15. (Apos. p. 266.) The Chief Engineer's log shows that the cargo was out of the 'tween-deck at 5 P. M. of that day. (Apos. p. 212.) The Pacific Mail Company's surveyor, Dupuy, was



on board from 5:30 P. M. to 6 P. M. Monday (Apos. p. 529), and examined all of the valves in the 'tween-deck (Apos. pp. 530, et seq.) so that all of the cargo must have been out of the 'tween-deck at that time. Also the Pacific Mail Company's witness Smith (Lloyd's surveyor) testified that he examined the starboard clapper-valve at 5 P. M. on Monday. (Apos. p. 563.) So that, if the vessel was made fast and preparation made for unloading as early as 11 A. M. Monday and the 'tween-deck was finished at 5 P. M., taking an hour off for noon it would leave 6 hours time for discharging all of that cargo in its damaged condition. The allowance of 4 hours to move and repair sufficient cargo to get at the clapper-valves aft in the 'tween-deck in the state of loading it was at 3 P. M. on Friday, October 12, seems especially liberal in view of these facts. The cost of so doing would have been very trifling in comparison to the probable damage which would be caused by water flowing in through one or both of those clapper-valves, if open.

Where it was discovered that the bonnet was left off of a clapper-valve in No. 2 hold, the other two in that hold being covered with cargo, and thereafter such clapper-valves in other holds as were not covered by cargo, were found in order, an ordinarily prudent person would naturally conclude that the Bethlehem Corporation had overlooked the valves in that hold—not that it had fixed two valves in that hold and happened to overlook the one, which did not happen to be covered with cargo at the time that

its defective condition was discovered. This is not looking at the situation in retrospect.

In any event the situation ought not to be held such as to permit the Pacific Mail Company to speculate at the expense of the Bethlehem Corporation, especially when a mere telephone call would have placed the decision squarely up to the latter. If the bonnets were on those two clapper-valves, all would be well and good, and the Pacific Mail Company would save itself the trouble of inspecting them at a time when it was somewhat inconvenient to do so. On the other hand, if the bonnets were not on those clapper-valves, then, the Bethlehem Corporation would pay for any cargo which might be damaged. Thus there would be no benefit to the Pacific Mail Company whatever in taking the trouble to confirm the belief in regard to the condition of those clapper-valves, and if there was any detriment the burden would fall upon the Bethlehem Corporation.

The Pacific Mail Company felt that First Officer Dowdy ought to have known that water might enter through the other two valves in No. 2 hold, and that he should have taken some action to prevent the probable damage to cargo stowed in that hold. This is apparent from the fact that he lost his job as First Officer on the return trip of the "Ecuador," and he was reduced to the position of a checker on the pier. He is now a relieving officer—in other words, a watchman. (Dowdy, *Apos.* pp. 272, 273.)

The duty to prevent further damage was again violated by the Pacific Mail Company, in that, with additional knowledge of facts sufficient in themselves to put that Company upon inquiry, the damages over and above the trifling cost of repairing the clapper-valves, as called for by the contract, again could have been prevented by reasonable endeavor and exertion.

The "Ecuador" set out on her voyage at 10:20 P. M., October 13, 1923. Nothing out of the ordinary occurred until 10 P. M. Sunday, October 14th, when the quartermaster, Puddu, took soundings and found 35 inches of water on the sounding rod in No. 2 port bilge (Apos. p. 364), and this was reported to the master, Captain Boyce (Apos. p. 167), by the Second Officer Sutter, who was then on watch (Apos. p. 338). The prior soundings, taken about 5 o'clock, showed that there were 6 inches of water in that bilge, so that at 10 P. M. Sunday the vessel's officers knew that water was flowing into No. 2 hold at a rapid rate, and had reached an extraordinary height, as Captain Boyce testified it was then only 6 or 8 inches from the cargo. (Apos. p. 168.)

CAPTAIN BOYCE (Apos. p. 208):

"Q. Didn't you say, captain, that it is a very unusual thing to find 35 inches of water in the hold?

A. Unusual, yes."

QUARTERMASTER CHRISTENSON (Apos. pp. 332, 333):



“Q. Did you ever hear in any of the vessels in which you have been of as much as 35 inches of water being in their holds, as a usual and customary thing?

A. No.

Q. That is very unusual, isn't it; that is very unusual, isn't it? Just look at me Mr. Christenson: That is very unusual, isn't it?

A. I don't know, but I guess it is; I couldn't say.

Q. If you are making soundings, sounding a hold, and find 35 inches of water in it, you would instantly know that something was wrong, wouldn't you?

A. I would report to the officer on watch if I was in doubt whether there was something wrong.

Q. You would not be in doubt about that at all, would you? You would know immediately, wouldn't you, if you found there were 35 inches of water in a hold that there was something wrong?

A. I should think so.”

PILLSBURY (Expert witness for Pacific Mail Company, Apos. p. 515):

“Q. \* \* \* That was an unusual amount of water in her hold, wasn't it?

A. Yes.

Q. That amount of water in her hold indicated something serious being the matter, didn't it?

A. Yes.”

Chief Engineer Murray admitted that it was an unusual thing to have 35 inches of water in a bilge, but would not say it was serious, although he believed that if it reached 40 inches, it would come in contact with the cargo (Apos. p. 463). No doubt

Mr. Murray meant that it would not be a serious thing as far as the possibility of sinking the vessel was concerned, because it certainly would be serious for the cargo. The only person to whom such an amount of water in the hold did not mean that there was something wrong was Third Officer Erickson (Apos. p. 310) on the 12 to 4 watch Monday morning. He was discharged, however, when the vessel returned from her voyage (Apos. p. 311), and has not worked since. (Apos. p. 316.)

But the statements of both Captain Boyce and Chief Engineer Murray that the water was 5 or 6 inches from the cargo at 10:00 P. M. Sunday are incorrect. The exact measurements show that the bilge tank tops were 36 inches from the bottom of the vessel and the cement in the bottom was 6 inches deep, leaving 30 inches as the depth of the bilge tanks. That in taking soundings the sounding rod came 9 inches from the cement bottom of the tank, so that when a sounding showed 35 inches of water in the bilge there were in fact 44 inches in the bilge. But the bilge was only 30 inches deep so there were 14 inches of water over the tank tops and in the cargo space of No. 2 hold at 10:00 P. M. Sunday (Murray Apos. pp. 444, 445, 446).

The following excerpt is from the testimony of Murray (Apos. pp. 445, 446) in reference to his sketch showing the bilge and sounding pipes:

“A. The top of the tank would be 36 inches above the bottom of the ship, 30 inches above the cement in the bilge.

Q. So that there would be a free space for water in the bilges on both port and starboard sides of a clear 30 inches?

A. 30 inches.

Q. And when your sounding-rod on the port side indicated 36 inches, there would at that moment, have been six inches of water over the double bottom tanks and into the cargo space; is that correct?

A. When your sounding board (rod) would indicate 36 inches, there would be actually 45 inches in the bilge, from the bottom of the bilge.

Mr. LILLYCK. We offer this sketch as our next exhibit."

(The document was here marked Bethlehem Shipbuilding Company, Third Party, Exhibit "I".)

With this knowledge on the part of the vessel's officers in ample time it cannot reasonably be denied that it was their duty then and there to take every precaution in order to prevent the cargo from being injured by sea water. Common prudence demanded that carefully checked soundings be taken frequently thereafter in order to ascertain the rate at which the sea water was entering the hold and its height kept down to the proper limit at all times by the use of the pumps. Its source also could have been ascertained, as there were only two ways in which the sea water could have entered the hold under the circumstances. One through the bilge pipes from the engine-room and the other from the clapper-valves. The former could have been checked in the engine-room, leaving the clapper-valves the only source. The starboard aft clapper-



valve was the only one under the water in No. 2 hold, and as it was known that a bonnet had been left off of another valve in that hold, the problem was an easy one and its solution just as easy. It is clearly apparent that the "Ecuador's" pumps could have taken care of all of the water that flowed in through the starboard clapper-valve.

The outside opening in that valve was  $2\frac{5}{8}$  inches in diameter. (Witness Dupuy, Apos. p. 534.) Second Engineer Morend testified that there were two four-inch pipes on the pumps into the bilge on each side. (Apos. p. 383.) Chief Engineer Murray testified that the pipes into each bilge were  $2\frac{1}{2}$  inches in diameter and both ran into a common suction pipe  $3\frac{1}{2}$  inches in diameter at the manifold in the engine-room. (Apos. p. 451.) That the pumping areas of the common suction pipe and the two bilge pipes combined were practically the same. (Apos. p. 456.) Taking Mr. Murray's testimony as correct, it ought not to need much argument to support the statement that the two  $2\frac{1}{2}$  inch bilge pipes, with efficient pumps, could have taken care of all water that flowed in through the starboard clapper-valve in No. 2 hold, had they been put on at the proper time. This is admitted by the Pacific Mail Company's witnesses Murray (Apos. p. 468) and Pillsbury. (Apos. pp. 520, 521.) The testimony of the Bethlehem Corporation's witnesses was to the same effect (Barker, Apos. p. 590; Muller, Apos. p. 668; Stoddart, Apos. p. 725).

The ability of the pumps and bilge lines to pump out all of the water as fast as it came in through the clapper-valve is shown in another way. It appears that the port valves in No. 2 hold were at least 3 feet above the water line (Apos. p. 188) and 6 feet above the floor of the 'tween-deck. The starboard valve was  $2\frac{1}{2}$  feet above the floor of the 'tween-deck, which would make the latter valve  $3\frac{1}{2}$  feet lower than those on the port side; they being 3 feet at least above the water line would make the starboard valve  $\frac{1}{2}$  foot below the water line. First Officer Dowdy said it was several feet. He was not sure how many, but when asked for his best judgment answered  $3\frac{1}{2}$  feet below the water line. (Apos. p. 301.) Chief Engineer Murray was doubtful, but estimated it at about 3 feet below the water line. The Bethlehem Corporation's witness Barker sighted along a line of the vessel determined by her fore and aft drafts when she set out on her voyage and concluded that the starboard valve in No. 2 hold would be just about at the water's edge.

Assuming that it was as much as 3 feet below the water line, the water would have flowed in at the rate of approximately 30 tons per hour. (Pacific Mail Company's expert witness Dupuy, Apos. p. 537.) The exact number of tons might be as much as a ton or so more or less than 30 tons per hour, due to the rolling of the vessel and motion through the water, if those elements would effect the amount of the inflow either way.

The Bethlehem Corporation's expert witness Muller testified that under a three-foot head the water would flow through the starboard clapper-valve at the rate of 30.7 tons per hour (Apos. p. 661), and expert witness Stoddart, also for the Bethlehem Corporation, gave as his estimate 32.3 tons per hour under a three-foot head. (Apos. p. 721.)

Chief Engineer Murray was asked how many gallons of water could be discharged a minute with both of the donkey pumps and the main-line engine pump running on the bilge lines in No. 2 hold. He evaded the question several times and finally said that he had never figured it out (Apos. p. 476), but that about 100 tons of water per hour could be pumped with the ballast pump from the deep tank with a six-inch pipe running into that tank.

CHIEF ENGINEER MURRAY (Apos. p. 477):

"Q. Then by pumping on one of those six-inch pipes you can pump in or discharge 100 tons of water an hour?

A. Yes.

Q. An hour?

A. Yes.

Q. Then the circulation would be the comparison between two  $2\frac{1}{2}$  inch pipes and one six-inch pipe?

A. It would just be the ratio."

That comparison works out as follows:

9.8	
—	of 100 equals 35. 1, the number of tons per
28.2	



hour which could be pumped from No. 2 bilge with one pump. Two pumps could have been put on No. 2 bilge, however, and they were put on the following morning. (Murray, Apos. p. 477.) Two pumps were more efficient than one. That does not include the main-line pump, however, but refers to the two donkey pumps. We mention this because there is testimony in the record that two pumps could not be used on the bilge lines, as they would work against each other. That is only true of the main-line pump working with a donkey pump. The Pacific Mail Company's expert witness Smith, Lloyd Surveyor, testified that the pumps on No. 2 bilge were discharging approximately 60 to 70 tons per hour while the vessel was at Wilmington, with two pumps on those bilge lines. (Apos. p. 562.) We are quite safe in saying, then, that approximately twice as much water could have been discharged through the bilge lines than was entering at No. 2 hold through the clapper-valve.

Further proof appears in the vessel's log, too, of Monday, October 15th, that the pumps could and did take care of the inflow. If the engineer's log is accepted as correct, the ballast pumps were put on No. 2 bilge at 7 A. M. Monday, and discharged a good steady stream. The vessel was dry at 1 A. M. Tuesday, making the time 18 hours that the pumps were running, the first ten hours of which time the water was flowing in through the clapper-valve. (Apos. p. 212.) The smooth deck log says that orders were given to use the pumps at 6 A. M. Mon-

day (Apos. p. 213), making 19 hours that the pumps were running, the first 11 of which water was flowing into the hold. In either event, it sufficiently appears that the pumps could and did discharge more water than flowed in through the starboard clapper-valve.

Now, if the officers of the "Ecuador" ought to have known that water would, or was, entering through the clapper-valves in No. 2 hold, it was their duty to put the pumps on that hold and to keep the water out of that hold as fast as it flowed in. If they had knowledge of facts sufficient to put them upon inquiry, which in this case would have revealed the true situation, they will be charged with knowledge of that situation.

The District Court held in effect (Apos. pp. 791, 792) that because First Officer Dowdy, when he inspected No. 2 hold before the cargo was loaded therein, closed his eyes to the obvious, he should not be charged with knowledge of the defective clapper-valves. No notice is taken of the fact that other officers of the vessel inspected the hold prior to the loading of the cargo. That although the vessel's officers suspected that the other valves in No. 2 hold were defective, after discovering that one had not been repaired, they ought not to be charged with such knowledge because they did practically everything possible under the existing conditions, short of discharging cargo, and they also examined other accessible valves in other holds and found none defective. This "everything possible" excepts,

of course, the possibility of moving a sufficient amount of cargo in the half filled 'tween-deck of No. 2 hold in order to get at the other two clapper-valves, and also the possibility of obtaining information by telephone from the Bethlehem Corporation in reference to the condition of those other two valves. That because accessible valves in other holds were found in order, the Chief Engineer (and the Chief Officer) were justified in assuming that the two valves in No. 2 hold, where the third valve was found unrepaired, had been properly repaired. In other words, if a clapper-valve located in No. 2 hold is found defective that would lead to the conclusion that the clapper-valves in holds Nos. 1, 3 and 4 were defective, but if some of the clapper-valves in holds Nos. 1, 3 and 4 were examined and found in order that would lead to the conclusion that the other two clapper-valves in No. 2 hold had been properly repaired. We think that the proper conclusion would be the one made by Messrs. Murray & Dowdy that No. 2 hold had been missed by the Bethlehem Corporation.

Again, says the District Court (Apos. pp. 792, 793):

“It is likewise true that there were 35 inches of water in the bilges at 10 o'clock at night about 24 hours after the vessel left port. The captain, realizing that this was unusual, directed pumps to be put to work on the bilges at once and an extra sounding to be taken at midnight, and on retiring left word that he be called immediately if the amount of water should increase. At 12 o'clock that night the



sounding showed but 25 inches. Another sounding at 2 o'clock disclosed the same amount. *Later the pump sucked air, indicating that all water was out of the bilges."*

The District Court fell into error in finding that after 2 A. M., Monday, October 15th, the bilge pump sucked air indicating that all water was out of the bilges. The main-line pump was put on No. 2 bilge about 10:20 P. M. Sunday, the 14th, and sucked air at about 11:00 P. M. (McKenna, 3rd Engineer, on watch, Apos. p. 397.)

Thus, instead of keeping the pump on No. 2 bilge from 10 P. M. Sunday night until after 2 A. M. the following morning, and thereafter No. 2 hold suddenly filled with water to the depth of 20 feet, the facts are that the pump was only kept on that bilge about forty minutes, until 11 P. M., and one hour thereafter it had filled again to the depth of 25 inches, that is, 25 inches on the sounding rod. 34 inches of water had actually flowed into No. 2 hold during that hour, bringing it 4 inches over the tank tops and into the cargo space. (Murray, Apos. pp. 444, 445, 446.) If the District Court had not erred in this finding, it probably would have been very reluctant to impliedly hold that the officers of the "Ecuador" ought not to be charged with the knowledge that water was flowing into No. 2 hold at an unusual rate.

(Apos. p. 793):

"As before stated *even if there were negligence* here, it would be at most a breach of duty

to the shipper and not to the repairer of the vessel."

While we think that any one of the three set of circumstances heretofore discussed would be sufficient to charge the officers of the "Ecuador" with knowledge that further damage would result if action were not taken to keep down the inflow of water in No. 2 hold, still it was incorrect for the District Court to consider each set of circumstances separately and hold that each set, considered by itself, was insufficient to charge the vessel's officers with such knowledge. The whole situation should be regarded from its four corners. To summarize generally the officers of the "Ecuador" had knowledge of the following facts at 12 o'clock Sunday night. All of them had been down in No. 2 hold prior to the time that the cargo was loaded therein and went there for the purpose of making an inspection to see if the hold was in every way fit to receive cargo. If they did not observe that the bonnets of the clapper-valves were not fastened thereon, it is because they closed their eyes to what was a patent defect. Moreover, their attention was called to a clapper-valve in the 'tween-deck of No. 2 hold when that deck was partially loaded, and the daylight was shining through the side of the vessel through that clapper-valve. They knew, therefore, that one clapper-valve had been missed in the 'tween-deck of No. 2 hold and they had a strong suspicion that the other two in the aft end of that deck had been missed, as evidenced by their crawl-

ing over the cargo and attempting to examine them. At 10 o'clock Sunday night they knew that there were 44 inches of water in the bilge of No. 2 hold, 35 on the sounding rod, which brought it 14 inches above the bilge tank tops and into the cargo space. This was pumped out at 11 P. M. and at 12 P. M. they knew that 34 inches of water had flowed back into that hold, 25 inches on the sounding rod, within one hour.

On this state of facts we submit that the officers of the "Ecuador" ought to be charged with knowledge that at midnight, Sunday, water was flowing into No. 2 hold at a rapid rate, and we are not viewing the situation in retrospect when we further contend that they should have put the pump, or pumps, on that hold and kept the water down as fast as it flowed in. We have been unable to find any authority indicating that a contrary ruling should be made, and our attention has not been called to any by opposing counsel. On the other hand the following cases strongly support the contention here made by the Bethlehem Corporation.

In admiralty we find the rule applied to collision cases and holding that the failure of the injured vessel in failing to prevent further damage after the collision is the proximate cause of such damage and not the collision.

The case of *The Transfer* No. 8, 88 Fed. 551, was decided by Judge Brown of the Southern District of New York. In that case the barge "Maine" was



damaged through the mutual fault of the "No. 8" and the "Waterman", and was in a sinking condition. Thereafter the "Maine" was taken by the "Waterman" into deep water where she sank. It was held that the "Waterman" had such notice of the "Maine's" condition as to require the "Waterman" to beach her and the sum of \$1000.00 was charged to the "Waterman" because it was not the proximate result of the collision but due entirely to the "Waterman's" failure to prevent additional damages. The court said in reference to the master of the "Waterman" (p. 552):

"He saw those on board abandoning her; and this, with the fact that she was gradually sinking, was sufficient notice to him that she must speedily go down and could not probably reach Port Morris Creek."

In the *M. E. Luckenbach*, 200 Fed. 630, affirmed 214 Fed. 571, the tug "Luckenbach" was towing the loaded coal barges, "A. G. Ropes", "William H. Conner" and "Henry Endicott" in the order named. There was a slight collision between the "Ropes" and the schooner, "Hugh Kelley", and the "Ropes" cast off the "Conner" to permit the schooner to cross through the tow. The "Conner" dropped one of her two anchors, but some 15 or 20 minutes afterwards she stranded on a shoal some three-fourths of a mile from where she was cast off, and was lost with her cargo. The owners of the barge and the owners of the cargo libelled the tug "Luckenbach" for the loss of the barge and cargo.

The "Luckenbach" brought in the schooner, "Hugh Kelley", as a third party respondent. The "Luckenbach" was found in fault and solely responsible for the collision, but it was held that the "Luckenbach" was not liable for the damages caused by the loss of the "Conner" and cargo, for the reason that the proximate cause for that loss was the negligence of the "Conner's" master in not dropping both anchors, which, with sufficient chain, would have held the "Conner" against the action of the tide and wind.

The court said in reference to the failure of the "Conner's" master to take such precautions as his knowledge of the situation seemed to require, at the time that his barge was cast off, which would have prevented the loss of the barge and her cargo:

"The situation, then, appears to have been this: There was a collision between the schooner and the barge Ropes, in which, however, the contact was so slight that no damage was done to either vessel. Nevertheless the captain of the Ropes, in the exercise of what is conceded to have been a wise precaution under the circumstances, cast off the hawser connecting the two following barges.

It was the obvious duty of the captain of the Conner to anchor at once, even if he had not been signaled by the tug to do so. Eventually he did so, dropping his 3,500-pound port anchor. The evidence shows that the bottom was good for anchorage; and that the anchor put over should have sufficed to hold such a barge, if sufficient chain were put out. Nevertheless, about 15 minutes later the barge was carried by the tide and cast aground on a shoal spot nearly

three-quarters of a mile distant, with the 3,200-pound starboard anchor on board. The necessary conclusion is, either that the captain of the barge neglected to anchor until just before grounding, or that, although he did put over one anchor shortly after being cast off, the barge dragged on the anchor, and he neglected to give out sufficient chain, or, at all events, to put over his second anchor. In view of the irreconcilable conflict in the testimony, it is very difficult to determine just what happened. Evidently, Capt. Printz did not get his anchor down as quickly as he claims. But I believe that the barge dragged her anchor for a considerable part of the distance traversed, due to the action of the tide and swell on a short anchor chain. *In either event the neglect on the part of the captain of the barge to take the simple precautions which the situation required constitutes the proximate cause of the stranding.* It is not a case of concurrent fault on the part of the tug and the barge. The fault of the barge was not a contributing cause. It was, under the circumstances, the efficient and proximate cause of the damages claimed. The evidence shows that Capt. Printz had ample opportunity, after learning that his barge was adrift, to anchor her. There was nothing in the surrounding circumstances to cause any particular excitement on the part of an experienced mariner in the fact that his barge was cast adrift, and he was ordered to anchor. *It was a simple, obvious precaution, and called for the exercise of merely ordinary care. If Capt. Printz had exercised ordinary care, the barge would not have grounded."*

In *The Drill Boat No. 4*, 233 Fed. 589, a drill boat stationed over a ledge in a channel was sunk by the spuds, which held it in place, becoming



jammed in the housing as the tide fell. The watchman returned early the next morning and so did the day crew, but nothing was done to mark the sunken drill boat, which, at that time, was visible. Later in the day, however, due either to a rising of the tide, or the sinking of the drill boat in the mud, it became completely submerged and was struck by a steamer, the latter receiving severe injuries. The owner of the drill boat petitioned for limited liability, which petition was denied, not only on the ground that the drill boat was unseaworthy, but because the owner ought to have known that the drill boat would become submerged, because of the rising tide or settling in the mud, and he should have taken reasonable precautions to prevent injury to his own and other vessels by placing a marker to indicate the location of the drill boat when it became submerged.

The same rule is also applied in admiralty cases involving contracts between the vessel's owners and the shippers.

In *The Ocean Wave*, Fed. Cas. No. 10,416, a river steamer had a barge in tow, and the barge struck a bar in the river. The steamer attempted to push the barge off and in doing so the timber head on the barge was broken in, and a bolt was drawn, which held the timber head under the water line, allowing the water to enter the hold and damage the cargo. The owner defended upon the ground that the stranding was a danger of the river, which peril was excepted under the bill of lading. The

court held, however, that the captain knew of the broken timber head and ought to have known that water might enter the hold.

“The leak could have been discovered by going into the hatch, or by looking into either of the scuttle hatches, or by the use of pumps, which would take water out at two inches depth.”

The case of *The Guildhall*, 58 Fed. 796, was also decided by Judge Brown of the Southern District of New York. In that case, a libel was filed to recover for damage to cargo in barrels on a voyage from Rotterdam to New York. The vessel came into collision with another steamer and put into London for repairs. Thereafter she set sail for New York and encountered heavy weather on the voyage. The libelants contended that the damage was caused by the collision. The vessel owner contended that it was caused by the tempestuous weather. The court found that it was due primarily to the collision, but found it unnecessary to decide whether such damage was exempt under the bill of lading. This was for the reason that the vessel owner had not exercised due diligence in preventing further damage by inspecting the cargo when the vessel was under repairs in London and at a time when the owners knew that cargo in other holds had been damaged by the collision. The court says on pages 799 and 800:

“As to the loss subsequent to the collision, it appears that the barrels in question were stowed in hatch No. 3; that a very slight inspec-

tion, on removing the after hatches in London, would have shown that these casks were damaged and needed repair. Forward, the cargo was examined; and being found injured by the collision, about one-third of the whole cargo was discharged, warehoused, and reconditioned. No damage, however, having been suspected aft, that part of the ship where the libelant's goods were stowed was not examined. Hatches Nos. 3 and 4 were not opened. *Having notice of damage to the cargo by collision, it was at the vessel's risk that even the most superficial examination, by removal of the after hatches, was neglected.* This negligence is attributable to the owners."

The same rule prevails on the law side of the court.

In the case of *Pere-Marquette Railway Co. v. The Chicago & Eastern, etc., Railway Co.*, (C. C. A.) 255 Fed. 40, a shipper delivered a shipment of beans to the initial carrier, and a wrongful delivery was made by the connecting carrier, which made deliveries without requiring a surrender of the bills of lading. The shipper recovered judgment against the initial carrier, which sought indemnity from the connecting carrier. The carriers used two standard forms of bills of lading: One a straight bill of lading, which did not have to be surrendered before delivery of the goods, and the other an order bill of lading, which did have to be surrendered, and contained the words, "Consigned to order of .....". The initial carrier issued a way bill, but the way bill stated the consignee to be



"order of" a person named, other than the shipper. The connecting carrier contended that the initial carrier was not entitled to indemnity, because the initial carrier negligently failed to notify the connecting carrier that the shipping documents should be surrendered before delivery, and the trial court so held. The Appellate Court reversed this decision on the ground that the way bill issued sufficiently apprised the connecting carrier that there were outstanding, against those shipments, order bills of lading which should have been surrendered before the delivery of the shipment. The court says on page 42:

"If the truth is as stated by appellees' freight agent that from these waybills one familiar with such matters could not judge whether a straight or an order bill of lading was outstanding for the shipments, it would certainly suggest that, before treating them as straight bills of lading at the risk of entailing loss on the shipper or the initial carrier, *he make inquiry for the purpose of resolving the doubt according to the readily ascertainable facts.*"

The rule that a plaintiff will not be entitled to indemnity from one primarily liable, where he has knowledge of facts which are sufficient to put him upon notice in regard to the possible danger and further damage, is merely a corollary to the rule that it is the duty of a plaintiff to minimize a loss rather than to increase it.

The case of *McNeil, Higgins Co. v. Old Dominion S. S. Co.*, (C. C. A.) 235 Fed. 854, was an action at

law to recover damages arising out of the shipment of a car load of coffee from New York to Chicago. The shipment encountered the so-called Dayton flood and wind storm at Peru, Indiana, and the top of the car was blown off and the coffee was wet by the rain and flood. It was admitted that the storm encountered came within an excepted liability under the bill of lading, but the shipper based his action upon the carrier's failure to prevent further damage after the storm was encountered. The cargo of coffee was held by the carrier at Peru, then taken to Cincinnati and later to Chicago where its sale brought only a nominal sum. It appeared that if the coffee had been promptly cared for the damage would have been comparatively slight. The District Court directed a verdict for the defendant carrier, but this ruling was reversed on appeal, and a new trial ordered, on the ground that it was the duty of the carrier to exercise reasonable diligence to prevent further loss. In disposing of the defendant's claim that the coffee could not be forwarded promptly to its destination because the record, showing the name of the consignee and destination, was lost in the flood, the Appellate Court observed that such information was obtainable by the carrier; that the conductor of the train had that information in his train book; that the car was in a train that was obviously routed from East to West; that defendant also had available permanent records kept at Newport News, Va., which showed the destination of the car in question, and that plaintiff had

notified defendant's agent that he was expecting a car of coffee, and defendant notified plaintiff some seventeen days after the injury occurred that the car was in the flood at Peru.

And in the State Courts:

The case of *Alaska-Pacific Steamship Co. v. Sperry Flour Co.*, (Wash.) 211 Pac. 761, was the third appeal of that case to the Supreme Court of the State of Washington, and the same ruling was made each time. A workman of the steamship company walked out on the plank from the dock to a dolphin for the purpose of casting off the lines of the vessel. He was injured by the unsafe condition of the plank. The dock and dolphin were both owned by the flour company and the plank was furnished by it. The workman recovered judgment against the steamship company, which sought indemnity from the flour company. The court held that the plank approach was as much under the steamship company's control as the flour company's during the loading operation. That the swaying of the dolphin was known to the steamship company, and its probable effect upon the plank approach; hence, under those circumstances, with that knowledge, the failure of the steamship company to take proper precautions for preventing the injury was an independent act of negligence. The claim of the steamship company for indemnity was denied.

In the case of *Appalachian Corporation v. Brooklyn Cooperage Co.*, (La.) 91 So. 539, the court, in



allowing plaintiff to recover indemnity for injuries to its employee caused by a defective door owned by defendant, pointed out that the plaintiff was not in possession of the property, and could not be charged with knowledge of the defective condition of the door and had no opportunity to prevent the accident.

In the case of *Alaska Steamship Co. v. Pacific Coast Gypsum Co.*, (Wash.) 128 Pac. 654, the very basis of the decision was the question of plaintiff's knowledge of the defective condition of a loading appliance furnished by the defendant. It appeared that plaintiff had knowledge of facts sufficient to put it upon notice of the defect several weeks previous to the accident, by reason of the appliance having operated improperly, although nothing occurred on that day to indicate danger. The lower court held that under the circumstances the plaintiff's knowledge of the defect was conclusively established and granted defendant's motion for a nonsuit. The Supreme Court reversed the ruling on the grounds that while such previous knowledge was very persuasive, still, it was not conclusive.

In the case of *Larkin Company v. Terminal Warehouse Company*, 146 N. Y. S. 380 (affirmed 117 N. W. 1074), a lessee was held liable for the death of an employee caused by the defective construction of an elevator. The lease sought indemnity from the owner, but it was denied on the ground that the lessee ought to have known of the danger from the defective elevator, because, previous to the time in

question, the elevator had been moved from one floor while it was being unloaded on another floor and property had been damaged thereby. Nothing was done thereafter by plaintiff to prevent an accident occurring in a similar manner.

In the case of *Robertson v. Trammell*, (Texas) 83 S. W. 258, 265, it is stated as an express condition of the right to collect indemnity that plaintiff had no notice in time to guard against any damage which might be caused by the act of the party primarily liable, citing *San Antonio Gas Co. v. Singleton*, (Texas) 59 S. W. 920, and *Cooley on Torts*, pp. 166 to 168. The term "notice" must necessarily include "knowledge of facts sufficient to put a party upon notice"; otherwise, as heretofore pointed out, a plaintiff could prove that he had no notice by merely testifying that he closed his eyes to the obvious.

The Pacific Mail Company owed just as great a duty to prevent further damage from the defective clapper-valve, as it would have to any vessel with which the "Ecuador" might have come into collision, or to its shippers where cargo was injured by peril excepted under the bill of lading, or to any tortfeasor. The officers of the "Ecuador" at midnight, Sunday, October 14th, had knowledge of more facts sufficient to put them upon notice of the impending damage, and more of an opportunity to have prevented it, than any of the parties charged with that duty in the foregoing cases. They not only had notice of such facts but they actually

knew that water was entering No. 2 hold at a rapid rate and this, coupled with their knowledge of the fact that one clapper-valve in that hold had not been repaired, and their suspicion that the starboard clapper-valve, the only one under water in that hold, had not been repaired, makes their failure to have taken proper action to prevent further damage not only gross negligence, but almost wilful misconduct.

We think that the District Court would have been inclined to so hold had it not been so convinced that the negligence of the Pacific Mail Company in this particular was a breach only of its obligations to shippers. The District Court entirely overlooked the fact that the Pacific Mail Company owed duties on this occasion to both the shippers and to the Bethlehem Corporation. To the former it owed duties of inspection and soundings, regardless of its knowledge of any impending danger. To the latter it owed duties of inspection, soundings and the use of the bilge pumps immediately when the officers ought to have known, and did know, that water was entering No. 2 hold, and probably, as they suspected, through the starboard water valve. Even if the source of the leak were only a suspicion, though based on good reason, it could have been easily confirmed. The fact that the Pacific Mail Company breached duties of inspection and soundings which it owed only to the shipper prior to the voyage, and on the voyage, regardless of unusual circumstances, has no bearing whatever on



the liability of the Pacific Mail Company for its breach of duty to the Bethlehem Corporation to prevent further damage.

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### CONCLUSION.

There has been an air of mystery, as far as the evidence is concerned, on one point in this case which is essential to the Pacific Mail Company's cause of action. The burden is upon that company to prove that the water which entered the starboard clapper-valve damaged the libelant's cargo wherever it may have been stowed in No. 2 hold, if stowed in that hold at all.

As before noted the water flowed into the vessel through the starboard clapper-valve at the rate of approximately 30 tons per hour, which incidentally the vessel's pumps were amply able to take care of, and in fact could have discharged the water about twice as fast as it flowed in. Assuming that No. 2 hold was dry at 11 o'clock Sunday night when the pump sucked air, as testified by the Pacific Mail Company's witnesses, and making the assumption that the bonnet of the starboard clapper-valve came entirely off of that valve immediately after that time, the greatest amount of water which could possibly have entered through the clapper-valve from 11 o'clock Sunday night to 10 o'clock Monday morning, when the vessel docked at Wilmington, would be 330 tons. At that time, however, approximately 630 tons of water had entered the vessel as

determined between the difference of the drafts of the vessel when she left San Francisco, and when she arrived at Wilmington. (Dupuy, Apos. pp. 538, 539, 555.) Add to this the water pumped out of the vessel between 6 o'clock and 10 o'clock Monday morning at the rate of 60 to 70 tons per hour, say 65 tons per hour, or 260 tons, makes a total of about 890 tons of water which entered the vessel; approximately 330 tons of which was the most possible amount of water which could have entered through the clapper-valve. How the balance of about 560 tons entered the vessel has never been explained by any testimony; although the burden of making a satisfactory explanation was upon the Pacific Mail Company, for the reason that the burden was upon it to prove that the water which entered through the clapper-valve did the damage claimed, and for the further reason that the vessel was at sea, during the time in question, in the exclusive possession of the Pacific Mail Company and its employees.

We say that this element of the Pacific Mail Company's case was left hanging in the air, so to speak, but that is only in so far as the evidence is concerned. Every person who had anything to do with the trial of this case knows perfectly well how that excessive amount of water got into No. 2 hold. There were only two ways which it could have entered; one through the clapper-valve, and the other through the bilge lines. There is testimony in the record that if the new engineer on the "Ecuador"

standing water from midnight Sunday to 4 A. M. Monday, had left a sea valve open, or if the pump in the engine-room bilge were running, as it usually is, and the non-return valves in the bilge lines were defective, or not operating because dirt in the bilges from the cargo became wedged in the valves, water would flow through the bilge lines into No. 2 hold. (Pacific Mail Company's witness, Murray, Apos. pp. 478, 767, 768; Blackett, Apos. p. 775; Young, Apos. p. 780; Bethlehem Corporation's witnesses, Muller, Apos. p. 700; Stoddart, Apos. pp. 715, 716, 718.) The fact that about 890 tons of water flowed into No. 2 hold, and allowing about 330 tons for the greatest amount possible to flow in through the starboard clapper-valve, raises the question as to how the other approximate 560 tons flowed into No. 2 hold. The obvious answer is that, after the pumps were started at 6 o'clock Monday morning, and the water in No. 2 hold increased, nevertheless, some one woke up to the fact that a sea valve was open in the engine-room and shut it off. Then the water in No. 2 hold gradually receded. In any event the question is not answered by having the employees of the Pacific Mail Company take the witness stand and testify that the bilge lines to No. 2 hold were in perfect order after the hold had been flooded.

Independently, however, of the ultimate determination of that question the petition of the Pacific Mail Company must be denied. This is not a case permitting the application of the doctrine that the



Appellate Court will be reluctant to reverse the District Court on a finding of fact, because the District Court heard the witnesses testify and is better able to judge as to the truth of their testimony. The rule that in actions *ex contractu*, such as this, the Pacific Mail Company will be allowed as general damage the cost of putting the unrepaired clapper-valves in a condition as called for by the contract, presents purely a question of law, and it is raised by the petition of the Pacific Mail Company. The rule that in order to collect special damages, such as the damage claimed here, the burden is upon the Pacific Mail Company to prove circumstances showing that the Bethlehem Corporation accepted the liability for those damages, and damages arising from collateral contracts, as a condition of the repair contract. The Pacific Mail Company made no attempt to show any such circumstances, and consequently, the question does not involve the truthfulness of any witness' testimony. The rule that the Pacific Mail Company was required to make reasonable exertions to prevent further damage, raises the question of whether that company knew, or ought to have known, that water was entering No. 2 hold at a rapid rate, at least by midnight Sunday. The answer to that question depends solely upon the facts disclosed by the testimony of the Pacific Mail Company. There is no conflict in the evidence, and there could not have been, for the reason that the Pacific Mail Company's employees were the only ones present on the vessel during the voyage. The

facts disclosed by their own testimony show conclusively that they did have ample knowledge of the impending danger, and their total lack of diligence to prevent it.

There has not been a single reason advanced why this ship repairing company, the Bethlehem Corporation, should have liabilities forced upon it which it did not accept under its repair contract, nor were they contemplated in fixing the consideration named in that contract. Even if it be held that the Bethlehem Corporation occupies the position of an insurer, as defendant in an action for the breach of its repair contract, it ought not to be held liable for damages which could have been easily prevented by the Pacific Mail Company. The law and the equities of the case are squarely opposed to such liabilities, the infliction of which upon the Bethlehem Corporation might be characterized mildly as an injustice.

It is respectfully submitted that the decree of the District Court in this action should be reversed.

Dated, San Francisco,  
November 14, 1925.

WILSON & WILSON,  
CHAS. H. LOVELL,  
IRA S. LILLYCK,  
*Proctors for Appellant.*

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IN THE  
**United States Circuit Court of Appeals**  
FOR THE NINTH CIRCUIT

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BETHLEHEM SHIPBUILDING CORPORATION, LTD., a Corporation,

*Third Party Respondent and Appellant,*

VS.

PACIFIC MAIL STEAMSHIP COMPANY,  
a Corporation,

*Respondent and Appellee;*

JOSEPH GUTRADT COMPANY, a Corporation,

*Libelant and Appellee.*

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**PETITION OF APPELLANT BETHLEHEM  
SHIPBUILDING CORPORATION, LTD., FOR  
REHEARING.**

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WILSON & WILSON,  
CHARLES H. LOVELL,

Nevada Bank Building, San Francisco,

IRA S. LILICK,

Balfour Building, San Francisco,

*Proctors for Appellant.*

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FILED

MAR 16 1920

F. D. MONCKTON,





No. 4684.

IN THE

# United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

BETHLEHEM SHIPBUILDING CORPORATION, LTD., a Corporation,  
*Third Party Respondent and Appellant,*

VS.

PACIFIC MAIL STEAMSHIP COMPANY,  
a Corporation,

*Respondent and Appellee;*

JOSEPH GUTRADT COMPANY, a Corporation,

*Libelant and Appellee.*

## PETITION OF APPELLANT BETHLEHEM SHIPBUILDING CORPORATION, LTD., FOR REHEARING.

*To the Honorable the United States Circuit Court of Appeals for the Ninth Circuit:*

The appellant, Bethlehem Shipbuilding Corporation, Ltd., respectfully asks for a rehearing in this case.

As appears from the opinion affirming the judgment appealed from, this was a libel filed by the Joseph Gutradt Company, appellee here, against the Pacific Mail Steamship Company for damage to cargo. The Bethlehem Shipbuilding Corporation, Ltd., appellant, was a third party respondent, having been impleaded

by the Pacific Mail Steamship Company, which prayed for judgment over on the ground that the cause of the damage to the cargo was the Bethlehem Corporation's breach of a contract to repair the ship "Ecuador". The decree was in favor of the Gutradt Company, libellant, against the Pacific Mail Company with judgment over against the Bethlehem Corporation, and the Bethlehem Corporation appealed.

The appellant contracted with the Steamship Company to make certain repairs to the Steamship "Ecuador", and to deliver the vessel alongside the pier of the Steamship Company ready to load cargo before 6 a. m. of October 11, 1923. The vessel was delivered by appellant to the Steamship Company on October 11, 1923.

Two days later the Steamship Company contracted with the Gudradt Company to transport certain soap from San Francisco to Norfolk, Va., and such soap was loaded by the Steamship Company on the "Ecuador" for transportation to Norfolk. On the voyage the soap was damaged by water which entered the hold in which the soap was loaded.

The Gutradt Company accordingly sued the Steamship Company to recover for such damage. Thereupon the Steamship Company caused appellant to be impleaded as a defendant in the action.

The opinion holds that appellant failed to properly perform the work on the "Ecuador" in that appellant left a clapper valve uncovered, and that the damage to the soap was caused by water which found its way into the hold in which the soap was stored, through said uncovered clapper valve.



It is shown in the opinion that the Steamship Company, after receiving the vessel from appellant, loaded the soap into the hold in which it was damaged without making any examination whatever of the vessel to see if the particular clapper valve in question in such hold was uncovered, although its attention had been called by one of the stevedores engaged in loading the hold in which such clapper valve was situated, to the fact that another clapper valve in that hold was uncovered and that as a result of such failure to examine said particular clapper valve, the "Ecuador" sailed with that valve uncovered, and that the damage to the soap was the consequence of such negligence by the Steamship Company.

As stated in the opinion, the clapper valve has a bonnet or cover which must be properly placed for the successful operation of the valve, otherwise sea water would enter the hold. After discharging the cargo in hold No. 2, in which the particular clapper valve in question was located, at Wilmington, it was found, that the water was rushing into No. 2 hold because of the bonnet being off the starboard clapper valve through which the water rushed.

To quote from the opinion:

"When the ship was redelivered to the Pacific Mail Company the Bethlehem Shipbuilding Corporation had broken its contract by failing to repair the clapper valves in No. 2 hold and the mere statement of the fact that the defective clapper valve let the water in compels the view that the ship was unseaworthy. It, therefore, devolved upon the Steamship Company to show that due diligence was exercised to make the ship seaworthy under the pertinent provisions of the Bill

of Lading. As between the Pacific Mail Company and the Gutradt Company, the duty of making the ship seaworthy was a non-delegable one; hence the Steamship Company could not successfully defend on the ground that it had made the contract with the Shipbuilding Corporation to repair and overhaul the clapper valves unless it could also show that the Shipbuilding Corporation had performed its contract."

Although the opinion shows that the most cursory examination of the starboard clapper valve in No. 2 hold would have disclosed the fact that such clapper valve was uncovered, and thus finds that the damage to the soap was caused by the failure of the Steamship Company to inspect the starboard clapper valve, which permitted the hold containing the soap to be flooded, and that the Steamship Company was guilty of negligence in not making such examination, and that such negligence was the direct and immediate cause of the damage to the soap, without which negligence the damage could not have occurred, and that, therefore, the Steamship Company had no defense to the action, the opinion proceeds to hold that appellant, because of its remote negligence was properly held liable in this action to the Steamship Company for the damage thus sustained by the Gutradt Company.

There is no pretense in the record on this appeal that the Steamship Company has paid the Gutradt Company the damages thus sustained. On the contrary, the finding is that the damages have not been paid, and the judgment is for the amount of such damages.

It is respectfully submitted that on the facts stated

in the opinion the appellant is not liable to the Steamship Company for the damages thus sustained by the Gutradt Company, and that such nonliability exists for two reasons:

1. The damage to the soap having been caused by the negligence of the Steamship Company in sending the "Ecuador" on a voyage without having made an examination of the starboard clapper valve in question, it cannot look to the appellant for reimbursement for its negligence.

2. That if appellant could be held liable to the Steamship Company in any case for such damage, it cannot be held liable for such damage until and unless the same is actually paid by the Steamship Company to the Gutradt Company.

3. The court misconstrued the real issues between appellant and appellee.

If appellant is correct in the statements thus made, the opinion in this case is clearly erroneous upon its face.

The amount involved in this appeal is not very large, \$2,476.80, but the claim of the Gutradt Company is only one of a great many other similar claims, aggregating \$126,661.67, and the Steamship Company is now contending that the opinion in this case, if allowed to stand, will establish principles of law which will be applied against the appellant in the proceedings involving the other claims, a libel for which has already been filed in the District Court by appellee against appellant.

It is, therefore, important to appellant, as well as to this Court, that the opinion in this case, if incorrect, shall not be allowed to stand.



1. *The law enjoined upon the Steamship Company the duty of seeing that the clapper valves in hold No. 2 were properly covered and it could not relieve itself of such duty by any contract or arrangement with appellant.*

The United States Statutes declare that it shall not be lawful for the owner of any vessel transporting merchandise from or between ports of the United States and foreign ports to insert in any bill of lading any agreement whereby it shall be relieved from liability for loss or damage arising from negligence, fault or failure in properly loading of any merchandise committed to its charge.

27 U. S. Stats. L. 445;

6 Fed. Stats. Ann. (2d ed.), pp. 371, 376;

*The Calderon vs. Atlas S. S. Co.*, 170 U. S.

272;

*The Tampico*, (N. D. Cal.) 151 Fed. 689.

To permit the Steamship Company to escape liability for its deliberate disregard of its statutory duty to see that the "Ecuador" was seaworthy before it left San Francisco, by transferring such liability to the appellant, would, it seems to us, be to put a premium upon such violation of the law and to permit the Steamship Company to do indirectly what it could not do directly.

2. *It is an elementary principle of law that an agreement to indemnify a person against the consequences of a future violation of law is absolutely void.*

The rule is declared in California as follows:

An agreement to indemnify a person against an act thereafter to be done is void, if the act be known to such person at the time of doing it, to be unlawful.

Civ. Code, sec. 2773.

The contract between the Steamship Company and appellant was made in California and hence it is subject to the laws of California and to the code provision in question.

Had the contract between the Steamship Company and appellant expressly provided that appellant, after making the repairs, should deliver the "Ecuador" to the Steamship Company in a seaworthy condition, ready for loading of cargo, and that the Steamship Company should not make any examination of the holds of the vessel to ascertain if the vessel was seaworthy, and that appellant would hold the Steamship Company harmless against all liability for damages caused by the flooding of the holds by water entering the holds through the uncovered clapper valves, and had the Steamship Company, in reliance on such contract, refrained from examining the clapper valves, this Court would be compelled to hold that such contract was contrary to public policy and to the laws of the United States and of the State of California, and, therefore, wholly void.

And yet the opinion in this case clearly holds that

the contract between appellant and the Steamship Company is, in effect, precisely such a contract of indemnity, and that, because it is such a contract of indemnity, the Steamship Company may recover from appellant the amount of the damage to the Gutrad soap.

We believe no case can be found which in the remotest way affords any support for holding that, by the contract between appellant and the Steamship Company, appellant became bound to indemnify the Steamship Company against damage to cargo resulting from the Steamship Company's disregard of its statutory duty to see that the vessel was seaworthy before placing cargo in the holds.

In *Forsyth vs. Woods*, 11 Wall. 484, 487, it was said :

"The promise, if any, of the firm was to indemnify the defendant for doing an act planned and intended to enable his principal in the administration bond to commit a gross breach of trust. The arrangement was entered into in order that the partnership might obtain the possession of all the effects, goods, chattels, rights, and credits which had belonged to the intestate decedent, and which were assets that the administrator only had the right to hold. It was also a part of it that the administration should be conducted by the firm and not by the person to whom the probate court committed it. To this arrangement the defendant became a party, and he signed the bond in view of it, and in order that it might be carried out. This appears from the plea. It needs no argument to show that the transaction was against the policy of the law and plainly illegal."

Accordingly the judgment in favor of the indemnitor was affirmed.



In the present case the contract of appellant, as construed by the opinion, was to indemnify the Steamship Company against a gross breach of statutory duty.

We do not question the right of the owner of a vessel to be indemnified against damage to cargo caused by latent defects in the vessel which would not have been discovered by an examination of the vessel; but in this case the defects were open and visible, and their presence must have been observed had an examination been made of Hold No. 2 before cargo was stored in the hold.

In this case the judgment itself establishes that the Steamship Company was guilty of negligence in not examining the clapper valves in Hold No. 2 and that the damage to the Gutradt soap would not have occurred but for such neglect.

A person is not entitled to indemnity for payments made by him on a judgment against him for injuries to a third person, where it is apparent that the judgment was based on his own negligence or wrong, or that of his employees.

31 Corpus Juris, 450.

"That one cannot recover damages for an injury, to the commission of which he has directly contributed, is the rule of established law. It matters not whether that contribution consists in his participation in the direct cause of the injury or in his omission of duties which, if performed, would have prevented it. If his fault, whether of omission or commission, has been the proximate cause of the injury he is without remedy against one also in the wrong."

*Little vs. Hackett*, 116 U. S. 371.

Where an action against a party seeking indemnity from another involves the actual negligence of the defendant therein, the latter, indemnitor, cannot be required to defend the action and is not bound by the judgment therein.

*Con. H. M. L. M. Co. vs. Bradley*, 171 Mass.  
127.

In *Gregg vs. Page Belting Co.*, 69 N. H. 247, 46 Atlantic 26, the plaintiffs, whose elevator was operated by a belt, caused the belt to be repaired by the defendant. By reason of defects in the repairing of the belt the elevator of the plaintiffs fell, causing injuries to an employee of the plaintiffs. The employee sued the plaintiffs for damages upon the ground that the belt was not properly repaired, that the elevator was improperly constructed, and was improperly equipped. The belting company was notified by the employer, of the suit, and requested to defend it, but neglected to do so. The employee recovered judgment; the judgment was paid by the employers, who then sued the belting company to recover the amount of the judgment, basing their claim on the negligence of the defendant in repairing the belt. The trial court directed a verdict for the belting company and the employers appealed. Held: That the verdict of the jury established that both the employers and the belting company were negligent and that the employee would not have been injured if either plaintiffs or the belting company had exercised care and that, therefore, plaintiff could not recover from the belting company. The Court declaring the rule to be that where a per-

son injured recovers damages from the one who caused the injury, the latter cannot recover over against another whose negligence primarily caused the injuries, if the negligence of the party against whom judgment is recovered in any way contributed to the injuries.

In *Union Stock Yards Co. vs. C. B. & Q. R. Co.*, 196 U. S. 217, the defendant turned over to the plaintiff for switching to plaintiff's stock yard, a boxcar which was in bad condition, in that the nut above the wheel on the brake staff was not fastened on the wheel, but rested upon the wheel as though it was fastened thereon. Had an inspection been made, the fact that the nut was not fastened would have been discovered. A brakeman of the plaintiff, while handling the car, by reason of the looseness of the nut, was caused to fall from the car and received injuries. The employee sued the plaintiff to recover judgment on the ground that his injuries were received by reason of the negligence of the plaintiff's employer to inspect the car. Plaintiff having paid the judgment sued the railroad company for the damages sustained by it in being forced to pay the judgment. The case came before the Supreme Court on a certificate from the Circuit Court of Appeals propounding the following question:

"Is a Railroad Company which delivers a car in due order to the terminal company, that is under a contract to deliver it to its ultimate destination on his premises, for a fixed compensation to be paid to it by the Railroad Company, liable to the terminal company for the damages which the latter has been compelled to pay to one of its employees on account of injuries he sustained



while in the customary discharge of his duty of operating the car by reason of a defect in it, in a case in which the defect is discoverable upon reasonable inspection?"

This question the Supreme Court answered in the negative. In the opinion of the Supreme Court it is said:

"Coming to the further question to be determined here, the general principle of law is well settled that one of several wrongdoers cannot recover against another wrongdoer, although he may have been compelled to pay all the damages for the wrong done."

The opinion then proceeds to show that the cases in which it has been held that one wrongdoer who has paid a judgment for damages caused by its wrongful act, may recover the amount thus paid from the joint wrongdoer, were cases in which the other wrongdoer was the active cause of the injury, and the party who paid the judgment was not a participant in the wrongful act, and had nothing to do with such act, but was held liable because of its relation to the active wrongdoer, or to the property where the accident happened, such as cases where an employer is held liable for the wrongful act of its employee, done without its knowledge, and where a municipality is held liable for injuries caused by an obstruction on the street placed there by a property owner or other person without its knowledge. It is then stated by the Court that while it was the duty of the Railroad Company to have inspected the car and to have repaired the defect in the brake, it was also the duty of the plaintiff to have inspected the car and reported the defect in the brake.

The opinion then states as follows:

"In the present case the negligence of the parties has been of the same character. Both the Railroad Company and the Terminal Company failed, by proper inspection, to discover the defective brake. The Terminal Company, because of its fault has been held liable to one sustaining an injury thereby. I do not think the case comes within that exceptional class which permits one wrongdoer, who has been mulcted in damages, to recover indemnity contribution from another."

We respectfully submit that the decision just referred to and quoted from is conclusive in this case and that it is impossible to distinguish this case from that case, and that, therefore, the opinion in this case is erroneous.

Where a Railroad Company delivered one of its cars to another Railroad Company for delivery at point of destination on the latter's line, and a brakeman of the latter company is injured by falling from the car, caused by the giving away of a handhold, through decay of the wood to which it was attached, in an action by the injured employee against his employer, the receiving line, to recover damages for the injuries, the latter interpleaded the delivering line, making it a party defendant. Judgment was recovered by the employee against the defendant employer, and by the latter against the delivering line. Held: That by reason of the negligence of the receiving line, the delivering line was not liable over to the receiving line.

*G. H. & S. A. Ry. Co. vs. Naas*, 94 Tex. 255, 59 S. W. 870.

"The duty of a Railroad Company to inspect the cars of other roads, received by it, is enjoined by law, and its dereliction of duty, in the event of an injury to its employee from such cars, is the proximate cause of the hurt, and the negligence of the company delivering over the unsafe cars is a remote cause."

*Missouri, Kansas & Texas R. R. Co. vs. Merrill*, 65 Kan. 436, 70 Pac. 358.

Egan, a longshoreman, engaged at work for the Alaska P. S. S. Co., was injured while assisting in loading one of its steamers at the Sperry Flour Company dock in Tacoma harbor. The Flour Company owned and operated a flour mill on the waterfront and maintained thereat a dock and dolphin for the use of the shippers coming to its place for cargo. After the vessel was loaded the longshoreman was sent to cast off the vessel's line from the dolphin and in order to perform that duty walked on a plank from the shore to the dolphin, and while thus walking the plank slipped off the dolphin, causing the longshoreman to fall upon the rocks below and sustain injuries. Egan sued the Alaska P. S. S. Co. to recover damages for his injuries and recovered judgment which was paid by the Steamship Company. The Steamship Company then sued the Flour Company on the theory that the latter was obligated to furnish the Steamship Company and Egan, the longshoreman, a safe approach to the dolphin, which it had negligently failed to do, and that such negligence was the cause of Egan's injuries. Judgment went for the Flour Company and the Steamship Company appealed. Held: That both the Steamship Company and the Flour



Company were negligent and that the Steamship Company therefore could not recover over from the Flour Company.

*Alaska P. S. S. Co. vs. Sperry Flour Company*,  
182 Pac. 634;  
*Alaska P. S. S. Co. vs. Sperry Flour Company*,  
211 Pac. 762-763.

In *City of Tacoma vs. Bonnell*, (Wash.) 118 Pac. 642, the plaintiff City maintained a municipal electric power plant and a system of wires, consisting of high voltage and low voltage wires, the latter conveying electricity direct to consumers. The defendant carelessly caused a plank to fall on both systems of wires, thus causing the current from the high voltage wires to pass directly into the low voltage wires instead of through transformers, with the result that a person who came into contact with the low voltage wires received the current from the high voltage wires and was killed. The widow and minor children recovered a judgment against the City for the death, the judgment being based upon the claim of the widow and children that the death was caused by the negligence of the City in not protecting its low voltage wires from the possibility of thus receiving the current direct from the high voltage wires. The City, having paid the judgment, sued the defendant for reimbursement. Held: That the City was guilty of active negligence in maintaining its wires in such dangerous condition, and that the City and the defendant were joint wrongdoers, and that, therefore, the City was not entitled to contribution from the defendant.

As we have said, the judgment in this case establishes, and the opinion of this Court holds, that the Pacific Mail Steamship Company was negligent in not inspecting the clapper valves of Hold No. 2. Under the authorities to which we have just referred, it is clearly impossible, legally, for the Steamship Company to hold appellant liable to it for the damages it may be compelled to pay the Gutradt Company, because of its negligence.

*3. If the appellant can, by reason of the implied contract to indemnify the Steamship Company against damage to cargo, caused by failure of the latter to examine the clapper valves, be held liable to the Steamship Company, it can only be held liable in the event of actual payment of the damages by the Steamship Company, and such payment by the Steamship Company is a condition precedent to any right of action against the appellant.*

The right to sue for indemnity for damages resulting from negligence, misfeasance or malfeasance of another occurs only when payment has been actually made by the indemnified party.

31 Corpus Juris, p. 452;  
*Powers vs. Munger*, 52 Fed. 705;  
*San Joaquin Valley Bank vs. Gate City Oil Co.*, 36 Cal. App. 791;  
*Terry vs. Southwestern Building Co.*, 43 Cal. App. 372;  
*Dunn vs. Uvalde Asphalt Paving Co.*, 175 N. Y. 218, 67 N. E. 439.

3. (a) *The issue between the parties to this action on the question of damages is not whether the damages claimed naturally ensued from the breach of the contract for repairs.*

This Court ruled in its opinion that the appellant was liable to the Steamship Company for the damages claimed, because such damages naturally ensued from the breach of the contract for repairs. Appellant's contention was (Brief, pp. 5 to 35) that the damages were special and not general.

The ruling of the Court is in no way inconsistent with that contention, nor is it at all relevant, because both general and special damages naturally ensue from the breach of the contract. If it appears that the damages claimed are such damages as usually follow in the great multitude of similar cases, then the damages are classed as general and allowed as of course. It is a matter of common knowledge, as well as proved by the lack of cases, that failure to make repairs upon a vessel is not usually followed in the great multitude of such cases by damage to cargo. The present case is the only one of its kind where such a claim has ever been presented for decision. It follows, then, that the damages here claimed must necessarily be special damages, and in order to collect them the Steamship Company must make it appear by competent evidence that that liability was assumed by the appellant at the time that the agreement for the repairs was made. In other words, the circumstances must show that the assumption of such a liability was made a condition of the contract. That was the issue squarely framed between the appellant and the



Steamship Company, and in justice to our client we feel compelled to request the Court in this petition to pass on that issue.

One word more on that point. This action is purely for breach of contract, and we are not concerned with those cases based upon negligence, where the rule of damage is that the party guilty of negligence is liable for all damage caused by the negligent act which might reasonably have been anticipated. There is a very sharp distinction between the rule of damages in cases *ex contractu* and *ex delicto*.

3. (b) *The issue between the appellant and the Steamship Company was not whether the officers of the "Ecuador" were bound to anticipate a breach of the repair contract, and hence whether they were guilty of negligence.*

The contention of the appellant was that all of the officers of the vessel were in No. 2 hold prior to the time that any cargo was loaded therein, and that they could have seen that the valve was defective if they had looked. That their attention was called to one defective valve in that hold, and they could have ascertained by inspection, or by telephoning the appellant, the condition of the other valves in that hold. Furthermore, at the end of the first twenty-four hours that the vessel was on the voyage they knew that an excessive amount of water was flowing into No. 2 bilge, it then being over the bilge tops and into the cargo hold. The appellant argued that under those circumstances it should be held that the officers of the vessel knew, or ought to have known, that water was flowing into No. 2 hold, which should have been

kept down by the bilge pumps. In other words, by the exercise of reasonable exertion, called for by the facts of which they had notice, the damage to the cargo could have been prevented. This contention, we submit, is sound under the authorities on pages 71 to 82, inclusive, of our brief, and we believe that it is not squarely met by the ruling that the officers of the "Ecuador" were not bound to anticipate a breach of the repair contract, and, therefore, they were not guilty of negligence.

It is respectfully submitted that a rehearing should be granted in this case.

WILSON & WILSON,  
CHARLES H. LOVELL,  
IRA S. LILICK,  
*Proctors for Appellant.*





No. 4685.

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IN THE  
United States  
Circuit Court of Appeals,  
FOR THE NINTH CIRCUIT.

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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

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ANSWER TO PETITION FOR REHEARING.

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#### ANSWER TO PETITION FOR REHEARING.

Plaintiff in error in its petition for rehearing complains that this court "did not decide or pass upon the questions of law on the special findings of fact as presented and raised by subdivision 4, at page 76 of the brief of plaintiff in error". (Pet. for Rehearing, p. 4.)

In its opinion, after declaring that the bill of exceptions had been signed and certified in contravention of law, this court declared:



“The bill of exceptions must therefore be disregarded, and this leaves for consideration only the sufficiency of the complaint, and the sufficiency of the special findings to support the judgment.”

The closing paragraph of the opinion reads:

“In the face of these findings it cannot be seriously contended that the fraud of the secretary did not result in substantial loss to the Cotton Company. The complaint and findings amply support the judgment and the judgment is accordingly affirmed.”

Accordingly, it appears: first, that this court considered that “the sufficiency of the special findings to support the judgment” was one of the questions before it for decision; second, that “the findings amply supported the judgment”. Nothing further was required.

National Prohibition Cases, 253 U. S. 350, at 384;

Texas & Pacific Ry. Co. v. Hill, 237 U. S. 208, at 215.;

In states where there is a constitutional provision relating to the matter the courts are not required to assign reasons for every point decided.

People v. Burke, 18 Cal. App. 72, at 78.

“Indeed, it seems hardly practicable or requisite to notice specifically all of the grounds of attack upon the judgment to which our attention has been invited. The author of an opinion should, of course, keep in mind the constitutional provision requiring an appellate court to give reasons

for its conclusion, and should have a due regard for the gravity of the offense and the possible bearing of the opinion as a precedent in the future. He should also be not unmindful of the valuable assistance of counsel, but, manifestly, he must follow his own judgment as to the degree of elaboration to be accorded to the treatment of any proposition and as to the questions which are worthy of notice at all."

Garrett v. Weinberg, 59 S. C. 162; 37 S. E. 51, at 61.

"For this court to undertake to formulate the exceptions, subdivisions, and branches of subdivisions so as to state distinctly the points which the appellants claim arise upon the record of the case, would impose upon the court a duty not contemplated by the constitution, especially as the supreme court is required to file its decisions within 60 days from the last day of court at which the cases were heard. While this court has considered the exceptions, and decides that they cannot be sustained, it has not, on account of the facts just mentioned, stated its reasons in reaching said conclusion."

In its opinion the court, after pointing out that the sufficiency of the complaint and of the special findings to support the judgment were the only questions to be considered, declared:

"While these questions are raised by the assignments of errors unfortunately the assignments are discussed in the brief in connection with other assignments which depend upon the bill of ex-

ceptions and we are left somewhat in the dark as to the particular objections urged against the complaint and findings alone.”

To none of the many contentions urged by plaintiff in error is this declaration of the court more pertinent than to the contention made under subdivision 4, page 76 of the brief of plaintiff in error. Turning to page 76 of the brief of plaintiff in error we find that from assignments of error numbers 2, 25, 27, 28 and 30, the contention made under subdivision 4 is evolved. Turning to pages 35 to 47 of the brief of plaintiff in error, we find:

“1. Assignment number 2 specifies as error the action of the trial court in denying defendant’s motion for nonsuit.”

A consideration of this assignment involves an examination of the evidence.

“2. Assignments numbers 25 and 30 specify the insufficiency of the evidence to support the finding that the stock sale from West to Sears occurred on December 1, 1920.”

A consideration of these assignments involves an examination of the evidence.

“3. Assignment number 28 specifies that the judgment is ‘contrary to law and to the cause made and facts stated in the pleading and records in said action’.”

The phrase “the cause made” refers to the evidence introduced.



The declaration of the trial court [Tr. pp. 150-151] "*that for all practical purposes*" on and after December 1, 1920, the Cotton Company acted as a corporation sole, to wit: J. B. Sears, is not, as counsel for plaintiff in error contends, a finding of fact, but is the conclusion of the court from the findings of fact immediately preceding the statement of such conclusion. [Tr. p. 149.] Because of its conclusion that on December 1, 1920, Sears for all practical purposes became the corporation, the trial court, applying the principle laid down in the decisions cited by counsel for plaintiff in error in their brief, pages 81 to 95, inclusive, released the Surety Company from further liability upon the bond, although the evidence disclosed that subsequent to that date Sears continued his practices of fraud and deception to the great financial loss of the Cotton Company.

The principle announced and applied by the courts in the decisions cited by plaintiff in error is, to it, most favorably stated by plaintiff in error (Brief, p. 91) as follows:

"When a person whose conduct is insured ceases to be an employee within any fair and reasonable interpretation of the term used in the policy, the insurer's liability *should cease*, unless he has notice of the change."

This principle was applied by the trial court in releasing the plaintiff in error from further liability after December 1, 1920, at the time when, as the court concluded, Sears, the person whose conduct was in-

sured, ceased to be an employee and for all practical purposes became the corporation or employer.

Counsel for plaintiff in error, not satisfied with the application of the rule as contended for by it in the trial court and there applied to the facts found, now seeks for the first time before the appellate tribunal to have the principle ("when the employee becomes employer the insurer's liability should cease") added to and supplemented by the further proposition "and all existing liability shall be extinguished".

In other words, plaintiff in error seeks to have the principle given a retroactive effect so as to read "when the person whose conduct is insured ceases to be an employee within any fair and reasonable interpretation of the term used in the policy, the insured's liability shall cease, *and any existing liability of the insurer shall be extinguished.*"

A more pointed expression of the principle contended for by plaintiff in error is stated as follows:

"When the person whose conduct is insured ceases to be an employee within any fair and reasonable interpretation of the term used in the policy, the policy shall thereupon become cancelled *as of the date of its issuance*, unless the insurer elect to the contrary."

No authorities have been cited which sustain this contention of plaintiff in error.

The case cited by plaintiff in error (Farmers & Merchants State Bank v. U. S. Fidelity & Guaranty Company, 28 S. D. 315, 36 L. R. A. (N. S.) 1152) involving the acquisition by the risk of "ownership of a majority of the stock and control and management of an insured corporation", goes no further than to hold that the insurer is not liable for delinquencies of

the risk committed *after* such change in ownership and control. There is no intimation in that case that such a change has the effect of *releasing* the insurer from liabilities incurred *prior* to such change.

In the more recent case of *Bank of Willow Lakes v. Syverson*, 43 S. D. 295, 178 N. W. 989, the same court repudiated the doctrine, announced in the case of *Farmers & Merchants State Bank etc. v. U. S. Fidelity & Guaranty Company*, that change of ownership of stock exempted the insurer from liability for fraudulent acts on the part of the risk "committed after he had acquired control of the corporation", saying among other things:

"Must we not assume that the company did not consider possible changes of stock ownership as affecting the hazard involved, even though the same men whose integrity was guaranteed, and who constituted a majority of the stockholders, should choose to place themselves in active management and control of the affairs of the bank? May we not assume that the bonding company considered the hazard lessened rather than increased, when persons holding a majority of the stock, and therefore most heavily interested in the success or failure of the business should themselves choose to assume direct control and management of the affairs of the bank? Neither the application nor the policy in this case contains any warranties, express or implied, nor any representations, from which an inference of increased hazard may be drawn in case the employees whose integrity is guaranteed should become majority stockholders, and thereby invested with absolute and plenary management, control, and supervision of the affairs of the bank. *The application and policy constitute the entire contract between the bank and the company, and the courts are without*



*power to interpolate into it conditions wholly foreign to its express or implied provisions.* For this reason we are of the view that the case of Farmers & Merchants Bank v. U. S. Fidelity & Guaranty Co. should not be followed. This view renders it unnecessary to consider a number of collateral propositions urged by appellant's counsel, chief of which is that the defendant company would not have issued a policy, had it been advised that Syverson and Flindt had become the owners of a majority of the stock."

Notwithstanding this later decision, the learned judge of the trial court, as pointed out in the brief of defendants in error (page 96), applied the doctrine of the earlier South Dakota case and limited the recovery to the liability incurred before Sears purchased the stock of West. In our brief, pages 91 to 101, our position respecting this contention is more fully set forth.

The opinion of this court, as pointed out in the opening paragraphs of this answer, is a complete response to the petition for rehearing.

Because of our contentions as herein expressed and the absence of court rule providing for the filing of an answer to a petition for rehearing, we ask, in addition to the denial of the petition for rehearing, the indulgence of the court in the matter of this answer.

W. J. HUNSAKER,

E. W. BRITT,

T. B. COSGROVE,

*Attorneys for Defendant in Error.*

No. 4685.

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IN THE  
United States  
Circuit Court of Appeals,  
FOR THE NINTH CIRCUIT.

---

Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

---

PETITION FOR REHEARING.

---

W. S. BICKSLER,

W. C. SMITH,

DALE H. PARKE.

*Attorneys for Plaintiff in Error.*

---





No. 4685.

IN THE

United States

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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

PETITION FOR REHEARING.

*To the Honorable Judges of the United States Circuit Court of Appeals, for the Ninth Circuit:*

Your petitioner, Maryland Casualty Company, a corporation, plaintiff in error herein, respectfully petitions this court to grant your petitioner a rehearing, and for grounds thereof states:

Plaintiff in error contends that the trial court erred in its conclusions of law and in entering judgment for defendant in error on its special findings of fact; that this error is a plain error of law and such error was not

decided or passed upon by this court although duly presented by the record and by brief of plaintiff in error, all as herein more fully set forth and shown.

We quote from the opinion of this court as follows:

“The bill of exceptions must therefore be disregarded, and this leaves for consideration only the sufficiency of the complaint, *and the sufficiency of the special findings to support the judgment.* (Italics ours.) While these questions are raised by the assignments of error, unfortunately the assignments are discussed in the brief in connection with other assignments which depend upon the bill of exceptions and we are left somewhat in the dark as to the particular objections urged against the complaint and findings alone.”

The court in its opinion considered and passed upon the question raised by the brief as to the sufficiency of the complaint, but it did not decide or pass upon the questions of law on the special findings of fact as presented and raised by subdivision IV, at page 76, of the brief of plaintiff in error. This point which was raised and presented to this court is as follows, to-wit:

*“The Cotton Company during the latter part of 1920 became a corporation sole, to-wit: J. B. Sears, and thereafter J. B. Sears, the “risk” named in the bond, was in complete ownership and control of the Cotton Company. That on and after the date when such complete ownership and control was obtained by J. B. Sears, the Cotton Company, to-wit: J. B. Sears, had no right of action to recover for any loss sustained by the wrongful acts of J. B. Sears, whether committed prior to or subsequent to the date on which the ownership and control of the Cotton Company was acquired*

*by Sears. For that reason the trial court erred in finding judgment against the defendant and in refusing to grant defendant's motion for judgment for defendant. In view of the finding of fact that the Cotton Company became a corporation sole, to-wit: J. B. Sears, on December 1st, 1920, the trial court erred in its conclusion of law that the plaintiff (assignee for collection of the Cotton Company) was entitled to judgment for any loss resulting from the wrongful acts of J. B. Sears."*

The questions of law presented under subdivision IV, at page 76 in brief of plaintiff in error, were, as indicated by the opinion of this court, properly before this court for consideration.

Assignment of error number 27, found at page 47, in brief of plaintiff in error, is as follows:

"That the court erred in its conclusions of law in finding that the plaintiff is entitled to judgment against the defendant on its first cause of action in the sum of \$24,321.97, together with interest thereon, or any sum whatsoever."

The brief of plaintiff in error, at page 80, duly presented to this honorable court the fact that the trial court made a special finding of fact [Transcript of Record, page 149] that J. B. Sears on December 1st, 1920, purchased all the capital stock of the Cotton Company from T. J. West, and that after December 1st, 1920, the Cotton Company was a corporation sole, to-wit: J. B. Sears. Plaintiff in error urged at length in its brief that in view of this special finding it fol-



lowed as a matter of law that when Sears acquired the ownership of all of the stock of the Cotton Company he acquired and became the owner of any claims which the Cotton Company, to-wit: T. J. West, then had under the bond sued upon against the bonding company (plaintiff in error herein) and arising from his (Sears') wrongful acts; that the acquisition and ownership by Sears of all of the capital stock of said Cotton Company was at the same time the acquisition and ownership of any such claim based upon his own wrongful act, and that such acquisition of ownership of such claim thereby terminated all liability of the bonding company thereon; and that Sears, a corporation sole, doing business as the Cotton Company, or the defendant in error (assignee for collection) could not therefore legally enforce any such claims against the plaintiff in error herein.

Any claim on the bond, existing in favor of the Cotton Company prior to the date when Sears acquired ownership thereof and became the Cotton Company, a corporation sole, ceased to exist when owned by said Sears; that said claim was thereby terminated and extinguished; that thereafter there was not and could not be any claim which could be assigned to the defendant in error herein. The point of law was urged to this honorable court in the brief of plaintiff in error that a person can not have an enforceable claim against another person for loss resulting from his, claimant's, own wrongful acts; that, therefore, when Sears became the owner of such claim, as a corporation sole, he or

his assignee for collection could not maintain any action thereon. The findings of fact show that he was such corporation sole at the time of his death, and thereafter the corporation could not revive nor resuscitate any such claim against the plaintiff in error herein, nor by assignment thereof for collection give any rights whatever to the defendant in error herein. It need not be urged that the assignment of said claim to the defendant in error solely for the purpose of collection did not give it any greater right to enforce the same than existed in favor of J. B. Sears during his lifetime.

The law touching these questions was fully argued in brief of plaintiff in error, at page 81, and the statement thereof was and is as follows:

“The liability of the insurer is never greater than the liability of the risk to the insured. The merging of the risk (J. B. Sears) and the insured (Cotton Company) in the same person extinguished the claim and released the liability of the insurer.

“The sale by West, a corporation, to Sears, a corporation sole (the risk) released Sears as principal on the bond, which release discharged the surety.”

And the authorities to support the contentions of plaintiff in error are fully set forth on pages 81 to 95.

The foregoing points of law raised by the record and presented at length in the brief of plaintiff in error are based on the judgment roll, to-wit: on the special findings of fact and conclusions of law made and entered by the Honorable District Court and are not based or at all dependent upon the bill of exceptions.

Your petitioner herein respectfully contends that this court did not pass upon these points of law so raised and presented by plaintiff in error, no mention thereof being made in the opinion of this court in affirming the judgment.

Your petitioner respectfully contends that the trial court made a plain error of law in its said conclusion of law, to-wit: that the defendant in error was entitled to judgment so given, made and rendered in its favor; that this plain error was duly raised and presented to this court, and your petitioner respectfully submits that it is entitled to the opinion and judgment of this honorable court thereon, and that it is entitled to a rehearing and to a reconsideration of the points of law so raised and presented, and to a reversal of the judgment of the said District Court.

Respectfully submitted,

MARYLAND CASUALTY COMPANY, A CORPORATION,

By W. S. BICKSLER,

W. C. SMITH,

DALE H. PARKE.

*Its Attorneys.*



CERTIFICATE.

Come now the undersigned, W. S. Bicksler, W. C. Smith and Dale H. Parke, counsel for plaintiff in error, and certify that in our judgment the foregoing petition for rehearing is well founded in law and fact, and further certify that said petition is not interposed for delay.

..... W. S. Bicksler .....  
..... W. C. Smith .....  
..... Dale H. Parke .....



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IN THE  
United States  
Circuit Court of Appeals,  
FOR THE NINTH CIRCUIT.

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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

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BRIEF FOR DEFENDANT IN ERROR.

---

WM. J. HUNSAKER,

E. W. BRITT.

T. B. COSGROVE,

*Attorneys for Defendant in Error.*





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## **ERRATA.**

### **Transcript of Record:**

Page 431, lines 4 and 5, and page 432, lines 8 and 9, "twenty-nine thousand, three hundred thirty-seven and 99/100 (\$29,337.99) dollars" should read: "twenty-nine thousand, three hundred seventy-seven and 99/100 (\$29,377.99) dollars."

### **Brief of Plaintiff in Error:**

Page 12, line 11, "ninety-five" should read "ninety-five thousand."

Page 74, line 14, the figures "\$29,336.99" should read "\$29,377.99."

IN THE  
United States  
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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

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*Defendant in Error.*

---

BRIEF FOR DEFENDANT IN ERROR.

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Preliminary Statement.

In the brief of the plaintiff in error, at pages 7 to 21, appears what is termed "Statement of Case." It is preceded by: (1) a general statement entitled "History and Nature of the Case;" and (2) a subdivision entitled "Nature of Issues," which appears to be an attempt to state the issues raised by the complaint and answer. The general preliminary facts stated in the first subdivision, entitled "History and Nature of the Case," are somewhat helpful in approaching the matter presented for review. The so-called "Statement



of Case” and “Nature of Issues” are, however, as we view them after careful study and consideration, so entirely insufficient and incomplete as to cause confusion and misunderstanding in the mind of a reader not otherwise familiar with the questions involved and the manner in which they are raised. It is very doubtful if Rule 24 of this court is complied with in this regard; certainly the requirements of the rule are not strictly observed. Accordingly, we shall undertake the unusual burden for a defendant in error of presenting for the court’s consideration a concise abstract or statement of the case.

### Statement of the Case.

California Cotton & Factorage Company (hereafter called Cotton Company) applied for and the plaintiff in error (hereafter called Bonding Company) executed and delivered to the Cotton Company a fidelity bond agreeing to reimburse it for any loss (not exceeding \$50,000.00) of money, securities or other personal property, *including that for which it might be responsible to others*, which it might sustain by reason of any wrongful act of its secretary, J. B. Sears [Tr. pp. 121-125], who acted as general manager, with unrestricted authority to carry on the business affairs of the Cotton Company. [Tr. p. 126.]

The Cotton Company applied for and the defendant in error (hereafter called plaintiff Bank) extended to it a credit account in the amount of approximately \$200,000.00. [Tr. pp. 212-215.] The Cotton Company thereupon commenced to purchase cotton at various

points in California and Arizona, arranging for payment by means of sight drafts drawn against the Cotton Company in favor of the vendors and forwarded with cotton tickets (warehouse receipts) attached to the plaintiff Bank. Upon receipt of the sight drafts—cotton tickets attached—they were immediately presented to and accepted by the Cotton Company, acting through Sears [Tr. p. 127], and were then paid by the plaintiff Bank and held by it in its note department as bills receivable, the cotton tickets being attached as collateral. [Tr. p. 127.] Thereafter, ostensibly pursuant to the plan outlined at the time of the application for credit [Tr. pp. 212-215], but in reality, as found by the court, pursuant to a fraudulent scheme then entertained by him, Sears applied for and obtained the cotton tickets from the plaintiff Bank, giving in lieu thereof trust receipts [Tr. pp. 128, 129], then explaining and theretofore having explained [Tr. pp. 212-215] that in the event of a sale of the cotton it would be necessary to surrender the cotton tickets in order to make delivery of the cotton to common carriers for shipment to the purchasers, at the same time obtaining from the common carrier bills of lading which, with the accompanying sight drafts attached, would be returned to the defendant in error and the trust receipts taken up. [Tr. p. 130.]

Instead, however, of keeping his agreement and complying with the terms of the trust certificates, Sears, having sold the cotton and secured bills of lading, presented the same with sight drafts drawn upon the purchasers, to the plaintiff Bank, not, how-

ever, to the note department, but to officers unacquainted with the fact that the cotton covered by the sight drafts was cotton secured by Sears upon the faith of trust receipts then held by the Bank, and then obtained from such officers an O. K. or approval of the sight draft with bill of lading attached, so the same might be deposited as a cash transaction [Tr. pp. 131, 132]; Sears thereupon deposited the draft and attached bill of lading, as a cash item, in the plaintiff Bank to the credit of the Cotton Company, obtained a cash deposit entry in the Bank pass book of the Cotton Company, thereafter caused fraudulent entries to be made in the books of account of the Cotton Company indicating similar credits to its account, and falsified the records and accounts of the Cotton Company by carrying such amounts to the credit of the Company and failing to make any entries indicating the outstanding trust receipts. [Tr. pp. 133, 134.] Sears thereafter represented to the officers of the Cotton Company that he was making money, that the cash items so entered represented profits of the business and that the cotton tickets on hand represented profit. He also represented to the officers of the plaintiff Bank that he had not sold the cotton covered by the trust receipts, that the Cotton Company still had all such cotton tickets and that he could produce them upon demand. [Tr. pp. 134, 135.] In truth and in fact Sears had experienced great financial losses in the business transactions of the Cotton Company and had misapplied the moneys realized from the sale of the cotton covered by trust receipts to



liquidate such losses. [Tr. p. 136.] Sears died May 3, 1921, having committed suicide by shooting himself. [Tr. p. 188.] An audit of his accounts was immediately instituted [Tr. p. 237], which disclosed a shortage largely in excess of the amount of the bond. Notice was immediately given the plaintiff in error as required by the bond [Tr. pp. 237-256]; it denied liability [Tr. p. 267], whereupon an action was instituted by the defendant in error *as assignee* [Tr. p. 365], to enforce the penalty of the bond. Judgment in the amount of \$30,101.14 [Tr. p. 166] having been entered against the plaintiff in error, this writ is prosecuted.

## PLEADINGS.

### Complaint.

In the complaint as amended there was alleged (first cause of action) the identity of the parties [Tr. p. 16], the execution of the bond [Tr. pp. 16-21], the appointment of Sears as secretary of the Cotton Company, his performance of the duties of the office [Tr. pp. 22, 23]; the receipt between November 19, 1920, and April 25, 1921, by the plaintiff Bank of 87 sight drafts totaling \$82,487.96, to which were attached 1476 negotiable warehouse receipts, each for one bale of cotton; the acceptance in writing of the sight drafts by the Cotton Company, acting through Sears, the payment of the drafts by plaintiff Bank and the carrying of said accepted drafts upon its books as bills receivable and the warehouse receipts as collateral [Tr. pp. 40, 41]; that immediately following the receipt

of each of the various 87 sight drafts and warehouse receipts and the acceptance thereof by the Cotton Company, Sears on behalf of the Cotton Company applied to and secured from plaintiff Bank said 1476 warehouse receipts, substituting therefor 87 trust receipts under the terms of which, upon the sale of the cotton represented by the warehouse receipts, bills of lading (out-bound documents) covering shipment of the cotton would be returned to the bank in cancellation of the receipts [Tr. pp. 42, 43]; that Sears represented to the officers of plaintiff Bank that the sale of the cotton covered by the warehouse receipts necessitated the surrender of the warehouse receipts in order to obtain possession of the cotton for delivery of the same to common carriers for shipment, and that upon such exchange he would immediately return the bills of lading to the plaintiff Bank and take up the trust receipts. [Tr. pp. 43, 44.] That Sears, pursuant to a fraudulent scheme entertained by him, misappropriated and misapplied 1091 of said 1476 warehouse receipts and 1091 bales of cotton represented thereby, in the following manner: Having secured the warehouse receipts from defendant in error and given trust receipts therefor, Sears, acting as secretary of the Cotton Company, sold the cotton represented by the warehouse receipts and received bills of lading therefor and in violation of the terms of the trust receipts and his promises to the plaintiff, attached said bills of lading to sight drafts drawn against the purchasers of the cotton, presented the sight drafts with bills of lading attached to an officer of plaintiff Bank other

than the officer in charge of the note department, from which the warehouse receipts had been taken, and where the trust receipts had been deposited by Sears, and secured from said officer an O. K. or approval of the sight drafts with bills of lading attached, which enabled Sears to deposit the sight drafts to the credit of the Cotton Company as a cash item. That Sears thereupon deposited said O. K.'d or approved sight drafts with bills of lading attached as a cash item to the credit of said Cotton Company and obtained credit entries upon the bank passbook of the Cotton Company [Tr. pp. 44-47], and immediately thereafter caused entries to be made in the books of the Cotton Company showing the various amounts credited upon the bank passbook as standing to the credit of the Cotton Company without any offset or charge of any kind, and wilfully failed to make any entry in the books of the Cotton Company disclosing the nature of the transaction, the manner in which said credit account had been obtained, or the existence of the outstanding trust receipts, and thereafter represented to the officers of the Cotton Company that said credits so entered upon the bank passbook and the books of account of the Cotton Company represented funds made and accumulated by him in the conduct of the affairs of the Cotton Company, and upon inquiry made by representatives of plaintiff Bank, represented that the Cotton Company still retained, and that he as secretary of the Cotton Company then had in his custody in the vaults of said Cotton Company all and every the various warehouse receipts sur-



rendered to him by the plaintiff Bank for which it held trust receipts. [Tr. pp. 47, 48.] That said 1091 bales of cotton at the time of their disposition by Sears were of the value of \$60,628.72. [Tr. p. 48.] That between said dates Sears, pursuant to the said fraudulent scheme entertained by him and contemporaneous with the fraudulent conversions and misappropriations of the warehouse receipts and the cash represented thereby and the fraudulent representations made to the officers of the Cotton Company and plaintiff Bank, and while acting in his capacity as secretary of said Cotton Company, fraudulently misappropriated or misapplied the moneys wrongfully placed to the credit of the Cotton Company by using said moneys for the purpose of dealing and speculating in cotton, conducting such dealings and speculations at a loss, and paying such losses out of said moneys [Tr. p. 49]; that no part of said \$60,628.72 was used in the payment of any of said 87 acceptances held by plaintiff Bank.

That relying upon the false representations of Sears and the deceits practiced upon it by him, said Cotton Company permitted Sears to continue to act as secretary, and to conduct its business and incur indebtedness in its name. That said Cotton Company subsequent to said 19th day of November, 1920, would not have allowed Sears to continue in the position of secretary, nor to conduct any dealings on its behalf or to contract any financial obligations in its name had it known of the frauds and deceits being prac-

ticed upon it and upon plaintiff Bank by Sears. [Tr. pp. 50, 51.]

That because of said frauds and deceits of Sears the Cotton Company has sustained a loss, and has become and is responsible to plaintiff Bank in the amount of \$60,628.72. [Tr. p. 51.]

The suicide of Sears on May 3, 1921 [Tr. p. 30], notice of loss to the Bonding Company, as required by the terms of the bond [Tr. p. 29], refusal of the Bonding Company to reimburse the Cotton Company [Tr. p. 30], the entry of judgment May 9, 1922, in the amount of \$90,281.00 against the Cotton Company in favor of the plaintiff Bank upon the sight drafts and trust receipts [Tr. p. 30], and the assignment by the Cotton Company to plaintiff Bank of the bond and all rights of action thereunder [Tr. p. 31], are also alleged.

A second cause of action was set forth concerning which no questions are raised under the writ.

### **Answer.**

A demurrer to the complaint as amended having been overruled [Tr. p. 59], the Bonding Company answered, denying directly or for lack of information each of the allegations of the complaint as amended, save those establishing the identity of the parties, the issuance and currency of the bond, the unrestricted powers of Sears as secretary of the Cotton Company, and the entry of judgment against the Cotton Company in favor of the plaintiff Bank. [Tr. pp. 60 to 74.]

Several affirmative defenses were urged:

*First*, it was alleged that in the application for bond it was represented that there was no cash under the personal control of Sears, only as checks were issued or received for deposit, but that Sears as a matter of fact handled all the cash of the Cotton Company without being required to make an account therefor. [Tr. pp. 74-75.] *Second*, that the Cotton Company in its application for bond represented that all things would be paid by check, but that Sears was permitted to use cash in any manner he pleased. [Tr. pp. 75-76.] *Third*, that the Cotton Company represented in the application for bond that the checks and accounts would be checked up at least once each month by T. J. West, treasurer, but that as a matter of fact no audit was ever made by any person and no verification of the funds on hand was made, and that such audit, if made, would have revealed the loss complained of. [Tr. p. 76.] It was averred that all such representations were warranties and were a part of the bond and were broken in all the respects mentioned. [Tr. pp. 76-77.] *Fourth*, it was alleged that the bond required that the Cotton Company, within ten days after discovery of the dishonesty of Sears, notify the Bonding Company by telegram, and that no such notice was given. [Tr. pp. 78-79.] *Fifth*, it was alleged that the capital stock, save four shares, was owned by T. J. West, who on May 24, 1920, sold and delivered all of his stock to J. B. Sears, who thereafter continued to own the same until his death on May 3, 1921. [Tr. pp. 79-81.] *Sixth*, it was alleged that



the frauds and deceits of Sears complained of were fully known to the Cotton Company and all its officers; that the lien of the defendant-in-error upon the warehouse receipts was surrendered and extinguished; that upon the sale of the cotton represented by the warehouse receipts the bills of lading were returned to the defendant-in-error, who received full payment therefor, and that it sustained no loss by reason of any frauds of Sears. [Tr. p. 82.] *Seventh*, a supplemental answer was filed alleging that under the terms of the bond the employer (Cotton Company) was required to produce its books and records for investigation; that despite repeated demands so to do, said Cotton Company has refused to allow plaintiff-in-error to examine its records. [Tr. pp. 110-114.]

### Findings.

The court in special findings of fact [Tr. pp. 118, 155] found the allegations of the amended complaint respecting the first cause of action to be true, and the allegations of the various answers and special defenses of the plaintiff in error to be untrue, *excepting in this important particular*: the court found that on December 1, 1920, Sears purchased 496 of the 500 shares issued and outstanding of the capital stock of said Cotton Company and continued thereafter until his death to be the owner thereof [Tr. pp. 149-151], and that prior to said first day of December, 1920, Sears had wrongfully converted and misapplied cotton of the value of \$24,321.97. [Tr. pp. 152-154.]

## ARGUMENT.

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### I. MOTION TO STRIKE BILL OF EXCEPTIONS.

Defendant-in-error served and filed a motion to strike the bill of exceptions on the ground that the same has been signed and certified to this court in contravention of law.

Plaintiff-in-error anticipated this motion (Br. p. 25) and the question raised thereby is the first matter discussed in its brief. (Br. pp. 25-34.) Accordingly, at the outset we devote ourselves to a presentation of the points of fact and law submitted in support of our motion to dismiss and in reply to the argument thereon of the plaintiff-in-error.

#### Statement of the Facts.

The terms of the United States District Court for the Southern District of California, Southern Division, are held at Los Angeles on the second Monday in January and the second Monday in July of each year (Act of May 16, 1916, Chap. 122, Judicial Code, Sec. 72; Sec. 1057, U. S. Comp. Stats. 1916).

On March 9th, 1925, during the January term of the United States District Court held at Los Angeles, in an action at law tried before the court without a jury, judgment was entered in favor of the defendant-in-error (plaintiff below), and against the plaintiff-in-error (defendant below), in the amount of \$30,101.14. [Tr. p. 116.]

On March 14th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a stipulation, and from the court a special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including April 15th, 1925. [Tr. p. 514.]

On April 14th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a second stipulation, and from the court a second special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including May 15th, 1925. [Tr. p. 515.]

On May 15th, 1925, counsel for plaintiff-in-error secured from counsel for defendant-in-error a third stipulation, and from the court a third special order, extending and enlarging the time within which to prepare and file its bill of exceptions to and including June 15, 1925. [Tr. p. 517.]

On June 8th, 1925, plaintiff-in-error served upon counsel for defendant-in-error its proposed bill of exceptions [Tr. p. 187], and on June 10th, 1925, lodged the same with the clerk of the court. [Tr. p. 513.] This proposed bill consisted of 188 typewritten pages. [Tr. p. 187.]

On June 9th, 1925, by the written stipulation of counsel for the respective parties, the defendant-in-error was allowed to and including July 9, 1925, within which to propose amendments to the proposed bill of exceptions. [Tr. p. 518.]



On July 8, 1925, defendant-in-error served and lodged its proposed amendments. [Tr. p. 485.]

The writ of error herein was allowed, filed and entered on July 6, 1925. [Tr. p. 3.]

On Sunday, July 12, 1925, the term of court at which the judgment was entered expired. (Act May 16, 1916, Chap. 122, Judicial Code, Sec. 72; U. S. Comp. Stats., Sec. 1057.)

On July 22, 1925, counsel for defendant-in-error in writing advised counsel for plaintiff-in-error that the time for settlement of the bill of exceptions had expired. [Tr. p. 488.]

On July 24, 1925, plaintiff-in-error served written notice upon defendant-in-error that it would, on July 28, 1925, present the bill of exceptions for settlement. [Tr. pp. 519, 520.]

The matter of the settlement of the bill of exceptions came on for hearing upon said notice on said 27th day of July, 1925. [Tr. p. 482.]

The defendant-in-error thereupon filed its written objections and objected to the settlement of the proposed bill of exceptions on the ground that the court had lost jurisdiction to settle said bill, specifying the grounds of its objection in detail. [Tr. p. 493.]

In support of the motion to settle the bill the affidavit of Dale H. Parke, one of the attorneys for plaintiff-in-error, was presented and filed [Tr. p. 483], and the counter-affidavit of T. B. Cosgrove, one of the attorneys for defendant-in-error, was presented and filed. [Tr. p. 494.]

The affidavit in support of the motion recites the obtaining of three stipulations of counsel and three special orders of court extending the time to June 15th, 1925, within which to propose the bill, and the filing of the same June 10, 1925; the execution of a stipulation extending the time within which to propose amendments, and the filing of proposed amendments July 8, 1925, the checking of the proposed amendments by counsel for plaintiff-in-error, and his conclusion that they were for the greater part without merit; subsequent telephonic conversations with counsel for defendant-in-error, *no dates being given*, and admission of counsel for defendant-in-error that the proposed amendments were prepared by persons who were perhaps over-cautious, and suggesting that counsel for plaintiff-in-error indicate the proposed amendments he considered meritorious, and those he considered otherwise. The return on July 15, 1925, of plaintiff-in-error's draft of proposed amendments, with notations of counsel for plaintiff-in-error, accompanied by letter dated July 15, 1925, explaining check marks and notations made on copy of proposed amendments and requesting that counsel for defendant-in-error recheck proposed amendments, in view of comments of counsel for plaintiff-in-error respecting same, and indicating willingness of counsel for plaintiff-in-error to again recheck proposed amendments. Subsequent telephonic communications between July 15, 1925, and July 22, 1925, between counsel for respective parties, at which counsel for defendant-in-error stated he was rechecking the amendments and would be finished within a

day or two. The receipt on July 22, 1925, of a letter from counsel for defendant-in-error, returning plaintiff-in-error's copy of proposed amendments, advising counsel for plaintiff-in-error that the time for settling the bill of exceptions had expired, and that the court was without jurisdiction to settle the bill at that time; further stating that if the judge of the trial court took a contrary view of the matter certain suggested amendments would be waived while others would be insisted upon, and expressing a willingness to appear upon written notice at any time before the court to discuss the settlement of the proposed bill. Subsequent conference between counsel for the respective parties on July 23 and 24, rechecking the proposed amendments. That on June 9, 1925, request was made upon counsel for defendant-in-error to indicate what portions of exhibits he desired copied into the record, and statement by counsel for defendant-in-error that he would advise counsel for plaintiff-in-error as to the portions of said exhibits he desired copied into the bill. That counsel for defendant-in-error did not indicate the portions of the exhibits he desired copied into the bill of exceptions until July 25, 1925. The receipt on July 25, 1925, of communication from counsel for defendant-in-error reiterating opinion that time for settlement of bill of exceptions had expired, and that the court was without jurisdiction to settle the same, and suggesting manner of remedying certain defects in the proposed bill in order that question of settlement might be submitted to the court for decision. That sufficient time had not intervened between



July 8th and the end of the term within which to incorporate the proposed amendments. That subsequent to July 22, 1925, affiant had devoted practically his entire time in arriving at an agreement with counsel for defendant-in-error as to proposed amendments. That such agreement was not arrived at until the receipt of said letter of July 25. That the making of the corrections to the bill required a re-writing of a large portion thereof, the employment of a public stenographer on Friday, July 25, and the completion of same on July 27. That defendant-in-error proposed 296 amendments to the bill and later waived 121.

The affidavit of counsel for the defendant-in-error sets forth in chronological order the correspondence passing between counsel for the respective parties respecting the settlement of the bill of exceptions.

1. The first communication is that of July 15, 1925. It is from counsel for plaintiff-in-error to counsel for defendant-in-error. It returns plaintiff-in-error's copy of the proposed amendments and explains the check marks appearing thereon. It suggests a rechecking of the proposed amendments in view of the concessions and rejections of counsel for plaintiff-in-error, and further conferences looking to a settlement of the proposed bill.

2. The letter of July 22, 1925, from counsel for defendant-in-error in response to the letter of July 15, 1925. The opening paragraph of the letter calls attention to the fact that the time for settling the bill of exceptions had expired and that the court was

without jurisdiction to settle the same, but expresses a willingness, in the event the judge of the District Court takes a contrary view, to waive certain suggested amendments, and an intention to insist upon others, and closes with an expression of willingness to confer personally with counsel for defendant-in-error or to appear at any time before the trial judge to discuss the matter of the settlement of the proposed bill.

3. Letter dated July 24, 1925, from counsel for plaintiff-in-error to counsel for defendant-in-error, submitting copy of testimony of witness which had been omitted from the proposed bill of exceptions; also calling attention to service of notice of presentation of bill of exceptions, and further declaring that portions of the minutes and of the by-laws, as well as certain exhibits, are being made for incorporation into bill of exceptions as suggested by defendant-in-error.

4. Letter of July 25, 1925, from counsel for defendant-in-error to counsel for plaintiff-in-error, supplementing communication of July 22, reiterating opinion of counsel for defendant-in-error that the time for settlement of the bill of exceptions had expired and that the court was without jurisdiction to settle the same, and thereafter agreeing that in order that the proposed bill might be presented to the court and the question of settlement passed upon, certain suggestions were made regarding the contents of the proposed bill.

5. Letter of July 27, 1925, from counsel for plaintiff-in-error to counsel for defendant-in-error submitting copy of bill of exceptions as amended and requesting that the same be returned in good time in order that it may be presented to the court on the morning of July 28, 1925, for settlement.

6. The affidavit further recites that no stipulation, oral or written, was entered into between counsel for the respective parties extending the time for the settlement of the bill of exceptions beyond the expiration of the term in which judgment was entered, and that subsequent to the expiration of the term no stipulation was entered into between counsel for the respective parties consenting to the settlement of the bill of exceptions after the expiration of the term; that no order of the court has been made extending the time within which to settle said bill of exceptions beyond the term; that no motion or proceeding in said action was pending and undisposed of upon the termination of the term in which the judgment was entered; and that counsel for plaintiff-in-error had never requested counsel for defendant-in-error to stipulate extending the time to settle the bill of exceptions beyond said term. That the proposed amended bill consists of 257 pages.

The court took the matter under advisement, and thereafter, on July 29, 1925, filed its written order and opinion overruling the objections of the defendant-in-error, settling and allowing the bill of exceptions and allowing the defendant-in-error an exception to the ruling. [Tr. pp. 509, 510, 511.]



On July 30, 1925, the court filed a supplemental order to the order of July 29, 1925, amending the same by striking therefrom certain language inadvertently inserted. [Tr. p. 512.]

Thereafter, on July 31st, 1925 [Tr. p. 513], the bill of exceptions as amended, consisting of 257 pages—typewritten copy [Tr. p. 187]—was filed by the plaintiff-in-error as its engrossed bill of exceptions.

The defendant-in-error now moves to strike the bill of exceptions from the record on the ground that it was signed and certified to this court in contravention of law.

### Statement of the Law.

No order of court having been made, nor the consent of the defendant-in-error having been given, *during the term* or thereafter, extending the time within which to settle the bill of exceptions beyond the term in which the judgment was entered, and no motion for new trial or any other motion or proceeding in said action being undisposed of upon the expiration of said term, and no very extraordinary circumstances having been shown justifying the settlement of the bill of exceptions after the expiration of said term, the trial court lost jurisdiction of the matter and was without authority to settle the bill of exceptions.

1. Exporters of Manufacturers' Products v. Butterworth-Judsen Co., 258 U. S. 365.

Followed in:

- (1) Farm Mortgage & Loan Co. v. Willett, 285 Fed. 42, at 45;

- (2) Wick v. U. S., 290 Fed. 191;
- (3) Cirino v. American R. Co., 291 Fed. 569, 570;
- (4) Merchant v. Dairymen's League, 294 Fed. 281,  
at 282;
- (5) Greyerbiehl v. Hughes Electric Co., 294 Fed.  
802, at 807;
- (6) Stickel v. U. S., 294 Fed. 808, at 809;
- (7) Twohy Bros. v. Kennedy (Ninth Circuit), 295  
Fed. 462, at 463;
- (8) Goodwin v. U. S., 295 Fed. 856, at 857;
- (9) Ritz Carlton etc. Co. v. Gillespie, 1 F. (2d) 921,  
at 922;
- (10) A. T. & S. F. Ry. Co. v. Nichols (Ninth Cir-  
cuit), 2 F. (2d) 12, at 13.

Earlier decisions of the Supreme Court of the United States are to the same effect.

O'Connell v. U. S., 253 U. S. 142, 146;

Jennings v. Philadelphia, Baltimore & Wash-  
ington Ry. Co., 218 U. S. 255, 256;

Michigan Insurance Bank v. Eldred, 143 U. S.  
293, 298.

Consent of the opposite party should be express and not rest upon implication.

Jennings v. P. B. & W. Ry. Co., 218 U. S.  
255, 257-258.

"So grave a matter as the allowance of a bill of exceptions after the close of the term and after the court had lost all judicial power over the record should not rest upon a mere implication from silence. There should be express consent,

or conduct which should equitably estop the opposite party from denying that he had consented.”

The consent of the opposite party must be obtained during the term; even written consent after the expiration of the term will not revive the trial court's jurisdiction over the bill of exceptions.

Exporters etc. v. Butterworth-Judson Co.,  
*supra*;

Stickel v. U. S., 294 Fed. 808, 809.

The failure or neglect of plaintiff-in-error to apply to the court during the term at which judgment was entered for an extension of the term was not such a “very extraordinary circumstance” as to justify an exception to the rule.

Farm Mortgage & Loan Co. v. Willett, 285  
Fed. 42, 45.

[Note: The Circuit Court of Appeals (Second Circuit) denied a writ of mandamus to compel settlement and filing of the bill of exceptions and the Supreme Court of the United States thereafter refused to issue a writ of certiorari to review the decision of the Circuit Court of Appeals. Farm Mortgage & Loan Co. v. Hazel, 260 U. S. 733.]

Blisse v. U. S. 263 Fed. 961, at 963:

“In United Wrapping Machine Co. v. Stimson, 175 Fed. 1023, 99 C. C. A. 667 (1910), this court dismissed a writ of error; the bill of exceptions not having been signed within the term at which the cause was tried, and the court not having reserved control over the case by rule or order.



"In *Glickstein v. United States*, 215 Fed. 90, 131 C. C. A. 398 (1914), this court held that, where a defendant convicted of a crime *did not move to have his bill of exceptions signed* until after the expiration of the automatically extended time under rule 5, above referred to, the judge was without power to sign it. And we there said that: 'The extraordinary circumstances mentioned in the Supreme Court cases which justify the signing of the bill after the term has expired relate to circumstances which caused the delay, and cannot be said to include negligence of the party or the importance or difficulty of the question involved.' "

*Franklin County v. Furry*, 144 Fed. 663, at 664:

"The general rule is that a bill of exceptions must be filed during the term at which judgment is entered or within an extension of time granted during the term. If the party who prepares *and tenders* the bill is not at fault, delay that is occasioned by his adversary or by the act of the judge may be excused. \* \* \* But the fault here was that plaintiff-in-error *failed to present* to the trial judge for allowance and signature of a proper bill of exceptions until long after the expiration of the term and the filing of the record in this court."

Neither is the misunderstanding or lack of knowledge of the rule on the part of counsel such a "very extraordinary circumstance" as to justify an exception to the rule.

*Susquehanna Coal Co. v. Casualty Co. of America*, 247 Fed. 137.

[Note: The Circuit Court of Appeals (Second Circuit) denied a writ of mandamus to compel settlement and filing of the bill of exceptions.]

Prior to the decision of the Supreme Court of the United States in *Exporters etc. v. Butterworth-Judson Co.*, 258 U. S. 365, there was authority (dicta) to the effect "that such consent may be given even after the term has expired."

*Blisse v. U. S.*, 263 Fed. 961, 966;

*Exporters of Manufacturers' Products v. Butterworth-Judson Co.* (D. C.), 265 Fed. 907, 908.

[Note: The question before the District Court in the foregoing case was the identical question afterward submitted by the Circuit Court of Appeals (Second Circuit) to the Supreme Court of the United States under the provisions of section 239 U. S. Judicial Code (Comp. Stats., Sec. 1216). *Exporters of Manufacturers' Products v. Butterworth-Judson Co.*, 275 Fed. 1022.]

The duty of drawing up and seasonably tendering a bill of exceptions devolves upon the excepting party.

*Michigan Insurance Bank v. Eldred*, 143 U. S. 293, at 298-299.

"The duty of seasonably drawing up and tendering a bill of exceptions stating distinctly the rulings complained of and the exceptions taken to them, belongs to the excepting party, and not to the court. \* \* \* Any fault or omission in framing or tendering a bill of exceptions being the act of the party and not of the court, cannot

be amended at a subsequent term, as a misprison of the clerk in recording inaccurately or omitting to record an order of the court might be."

Disregard of the established rules of procedure through inadvertence of counsel, resulting in a defective bill, imposes upon the appellate tribunal the duty of following the mandatory provision of the statute and dismissing the bill.

Blisse v. U. S., 263 Fed. 961, at 961-962.

"We are not insensible to the fact that the dismissal of a cause without passing on the merits, because the inadvertence of counsel has disregarded an established rule or procedure, is to impose upon the litigant an extreme penalty. At the same time we are compelled to adhere to established rules of orderly procedure, which experience has shown to be important in the administration of justice. The rules respecting the preparation of a case to be brought to an appellate court on writ of error are not uncertain, and are not obscure, and it is to be assumed that they are familiar to counsel. A failure to observe them, as has frequently been remarked, only tends to confusion, and to the demoralization of the procedure of the court. *E. I. Du Pont de Nemours & Co. v. Smith*, 249 Fed. 409, 161 C. C. A. 377. To disregard such rules is to introduce uncertainty and perplexity into the administration of justice, and as Mr. Justice Story remarked is destructive of the law as a science. Story's Eq. Pl., Sec. 544."

*Oxford & Coast Line R. Co. v. Union Bank*,  
153 Fed. 723, at 728.



“While it is not the policy of the court to dismiss writs of error and cases of appeal on account of slight technicalities, at the same time the rules of this court, as well as the rules of the Circuit Court, are plain and easily understood. In this instance the provision of the statute relating to the question at issue is mandatory and must be enforced. It is incumbent upon attorneys who practice in the Federal Courts to observe and strictly follow the rules of practice and procedure in preparing and presenting bills of exceptions \* \* \*. It is essential to the orderly procedure of the courts that attorneys should comply with the rules relating to the same, otherwise it would be useless to promulgate rules for the guidance of those who may seek to review the action of the lower court.

“Mr. Justice Story in his work on Equity Pleading (section 544), in commenting upon the necessity of adhering strictly to the prescribed forms of procedure, says: ‘The want of due form constitutes a just objection to the proceedings in every court of justice, for to reject all form would be destructive of the law as a science and would introduce great uncertainty and perplexity in the administration of justice. Every irregularity of this sort is fraught with inconvenience and generally tends to delays and doubts, and it has been well remarked that infinite mischief has been produced by the facility of courts of justice in overlooking errors of form. It encourages carelessness and places ignorance too much on a footing with knowledge among those who practice the drawing of pleadings.’”

Mound Coal Co. v. Jeffrey Mfg. Co., 233 Fed. 913, at 919.

### Discussion.

Whatever doubt may have existed prior to the decision of the Supreme Court of the United States in the case of *Exporters of Manufacturers' Products v. Butterworth-Judson Co.*, 258 U. S. 365, as to the effect of proceedings had and taken subsequent to the expiration of the term, is dispelled by the language of the opinion in that case.

Not even express written stipulation of the parties executed subsequent to the term at which judgment was entered will legalize the settlement of the bill. In the present case not only is there no written stipulation consenting to the settlement of the bill subsequent to the term, but on the contrary the written communications affirmatively disclose a lack of consent.

During the term plaintiff-in-error obtained three special orders of the court and stipulations of counsel extending the time within which to propose the bill. None of these extended the time beyond the expiration of the term. Neither was any request made for a stipulation extending the time beyond the term. The remaining question presented upon this motion is: Do the facts occurring prior to the expiration of the term come within the meaning of the term "very extraordinary circumstances justifying the settlement of the bill after the expiration of the term"?

In order that it may have a correct understanding of the facts that occurred before and those that occurred subsequent to the expiration of the term, we invite the court's attention particularly to that por-

tion of the affidavit in support of the motion to settle the bill of exceptions appearing in the transcript at pages 485 to 488. This affidavit is not inartificially nor carelessly drawn; it is artfully and studiously prepared. We call attention to the fact that no attempt is made to set forth the dates of any occurrences transpiring between July 8 and July 15, although this is the important and controlling period—the term ending on Sunday, July 12th. The letter of July 15th, written by counsel for plaintiff-in-error, is the tie-point from which there is no escape. The affidavit declares that prior to the preparation of the letter of July 15th affiant had spoken with one of the attorneys for the defendant-in-error over the 'phone respecting the proposed amendments. No mention is made, however, of the date of this telephonic conversation. The nature of the conversation, however, as disclosed by the affidavit read in conjunction with the language of the letter of July 15th, would indicate that the telephonic conversation occurred immediately preceding the dictation of the letter. This appears particularly probable in view of the fact that the affidavit declares that affiant *had checked over* the proposed amendments and *found them to be without merit before he telephoned* to the attorney for the defendant-in-error, at which time he made known his views respecting the proposed amendments, whereupon counsel for the defendant-in-error suggested that the proposed amendments be check-marked to correspond with affiant's opinion of their merit or lack thereof. Compli-



ance with this suggestion was the letter of July 15, 1925.

The only circumstances occurring prior to the expiration of the term (Sunday, July 12, 1925) which in our opinion may be considered is the fact that between the time of the service of the proposed amendments and the expiration of the term, a period of three court days (four calendar days) intervened. At that time, as we view it, either one of two things occurred. Counsel for plaintiff-in-error either misunderstood the rule requiring the settlement of the bill during the term or some extension thereof obtained during the term, or understanding the rule they are guilty of negligence in failing to secure an order or stipulation extending the term. An abundance of time remained within which to secure a stipulation and special order of court of the character of any of the three theretofore given and made. Neither a misunderstanding of the rule, nor a neglect to obtain an extension of the term constituted "very extraordinary circumstances" justifying an exception to the rule.

We wish to emphasize what heretofore has been mentioned only casually, namely, that the proposed bill of exceptions served June 8th, 1925, and lodged with the clerk June 10th, 1925, consisting of 188 pages—typewritten copy [Tr. p. 187], was not the bill of exceptions served July 27, 1925, and settled by the court and filed with the clerk on July 31, 1925. The bill settled consisted of 257 pages—typewritten copy. [Tr. p. 187.] The difference in the original bill as proposed and the amended bill as settled was due to

an incorporation therein or addition thereto of 175 amendments proposed by defendant-in-error.

The plaintiff-in-error relies, among others, upon two decisions of the Circuit Court of Appeals for the Ninth Circuit. They are:

1. Sutherland v. Pearce, 186 Fed. 783;
2. Pacific Bank v. Hannah, 90 Fed. 72.

Concerning Sutherland v. Pearce, we direct the court's attention to the language of the opinion appearing on pages 786 and 787 of volume 186, Fed Rep., being subdivision 3. It discloses that on June 1, 1910, the court entered an order that the defendants should have four months within which to prepare and file for allowance their bill of exceptions. That *within this time* the bill of exceptions was filed and signed by the court, viz., on September 15, 1910.

Concerning Pacific Bank v. Hannah, 90 Fed. 72, we direct the court's attention to syllabus number one, reading:

"1. Bill of Exceptions.—Time for Allowance. The filing of a bill of exceptions during the term of court at which judgment is rendered is sufficient to preserve the rights of a party, and to authorize its allowance and settlement after the term."

The language of the opinion (90 Fed. 76) appears to bear out the statement appearing in the syllabus. It will be observed that no mention is made respecting an order of court or stipulation of counsel extending the time for settlement of the bill beyond the term. *As a matter of fact, there was such a stipu-*

*lation in the record*, concerning which more is said hereafter. Briefly referring to the authorities cited in support of the statement of the court, we have—

(a) *Woods v. Lindvall*, 48 Fed. 73.

In this case, at the term in which judgment was rendered, a *motion for new trial* was made. The motion for new trial *was not passed upon* until a subsequent term. The court in this manner retained jurisdiction of the action. At the term in which the motion for new trial was denied the bill of exceptions was settled. Passing upon this point, the court says:

“It is true that in several cases cited by counsel for defendant-in-error (citing Supreme Court decisions) it was held in effect that in the absence of an order of court extending the time a bill of exceptions covering errors committed at the trial cannot be allowed and filed (unless by consent of parties) after the term has expired at which the judgment was rendered. But in none of these cases did the question arise whether a bill of exceptions may not be allowed and filed at the term when the motion for a new trial is finally acted on, even though such action is taken at a term subsequent to the entry of judgment; *and that is the precise question which confronts us in the case at bar.*”

(b) *Waldron v. Waldron*, 156 U. S. 361.

The first syllabus reads:

“A bill of exceptions may be signed after the expiration of the term at which the judgment was rendered, *if done by agreement of parties made during that term.*”



The decision is by Mr. Justice White. At page 378 of the 156 U. S. Rep., the opening paragraph of the opinion reads:

“The signing of the bill of exceptions after the expiration of the term at which the judgment was rendered, was lawful if done by consent of parties given *during that term.*”

Citing, among others:

*Davis v. Patrick*, 122 U. S. 138,  
which was also cited in the Pacific Bank case.

(c) *U. S. v. Gotlieb Breitling*, 20 How. 252.

This decision is cited (Br. p. 29) by counsel for plaintiff-in-error.

This case, decided in 1857, holds that the general rule of a Circuit Court of the United States in Alabama, adopting the practice of the state courts in the matter of the settlement of bills of exceptions, is not binding upon the judges of said court. The decision also holds that the time within which to settle bills of exceptions must depend upon the rules and practice of the court and *on its own judicial discretion*. It is then declared:

“In the case before us, the judge who tried the case has deemed it his duty to seal and certify the exception to this court; and under the circumstances stated in the exception and the note, we think he was right in doing so, and that this exception is legally before this court as a part of the record of the proceedings of the court below.”

What was stated “in the exception and the note” the record does not disclose. Were the matters referred to in the “note” recited in the opinion of the court the correctness of the ruling might be at once manifest.

(d) Counsel for the defendant also refers to—

*Hume v. Bowie*, 148 U. S. 248.

At page 253 of the decision (148 U. S. Rep.) the court declares:

“The rule is unquestionably correctly laid down in *Muller v. Ehlers*, 91 U. S. 249, that when judgment has been rendered and the term expires, a bill of exceptions cannot be allowed, signed and filed as of the date of the trial, in the absence of any special circumstances in the case, and without the consent of the parties or any previous order of court. But it is always allowable, if the exceptions be seasonably taken and reserved, that they may be drawn out and signed by the judge afterwards, and the time within which this may be done must depend upon the rules and practice of the court and the judicial discretion of the presiding judge. *Dredge v. Forsyth*, 2 Black 563, and *Chateaugay Iron Company, Petitioner*, 128 U. S. 544. \* \* \*

“The rules also provided that the terms of court might be prolonged by adjournment for the purpose of settling bills of exceptions, *and an order was accordingly entered prolonging the term at which this judgment was rendered for the purpose of doing that in this case.* This was equivalent to the practice in many jurisdictions of entering an order granting additional time, after the

expiration of the term, in which to settle such bills.”

(e) *Dredge v. Forsyth*, 2 Black, U. S. 562.

This case was decided in 1862. Contention was made in this case that the exceptions must be drawn out and sealed by the judge *before the jury retires from the bar of the court*. The court held otherwise and declared (2 Black, U. S. 568):

“Great inconvenience would result from such a requirement, and in point of fact there is no such rule. On the contrary, it is always allowable, if the exception be seasonably taken and reserved, that it may be drawn out in form and sealed by the judge afterward, and the time within which it may be so drawn out and presented to the court must depend on the rules and the practice of the court and the judicial discretion of the presiding justice. Such was the rule laid down by this court in *U. S. v. Brietling* (20 How. 254), and we see no reason to qualify it on the present occasion.”

By the statement, “the time within which” the bill of exceptions may be presented to the court “must depend on the rules and practice of the court and the judicial discretion of the presiding justice,” is meant precisely what is stated, namely, that the presiding justice may, in his discretion, allow such time as he sees fit to settle the bill of exceptions. If the term expires, however, without any such order of the court having been made, then, according to the authorities (*Exporters’ etc. v. Butterworth-Judson Co.*, *supra*, it



is too late after the term has expired to obtain such order.

(f) *Chateaugay Ore & Iron Company, Petitioner*,  
128 U. S. 544.

This case is cited and is relied upon by plaintiff-in-error (Br. p. 30). At page 556 of the opinion (128 U. S.), the court, in declaring that upon the facts of the case then under consideration the decision in a leading case, namely, *Muller v. Ehlers*, 91 U. S. 249, had no application, uses this language:

“That decision has no application to the present case because the rights of the defendant were saved by the express order of the court, made *during the term*, and by a sufficient compliance on the part of the defendant with the rules of the Circuit Court, and by what must be held to have been the consent of the plaintiff.”

Accordingly, it appears that there was an express order of the court made during the term extending the time within which to settle the bill of exceptions. That, in the next place, there was a compliance with the rules of the court, and in the third place the facts indicated that the plaintiff consented to the extension. In the present case there is no order, express or implied, of the court made during the term extending the time to settle the bill of exceptions beyond the term. There is no consent on our part to such an extension, but on the contrary an objection was raised by defendant-in-error at the first opportunity following the expiration of the term, and persisted in thereafter.

This analysis of the authorities cited by Circuit Judge Morrow in the *Pacific Bank v. Hannah* case (90 Fed 72) discloses that in *each* of the authorities relied upon—save perhaps the possible exceptions of the case of *U. S. v. Breitling*, 20 How. 252, where special circumstances not set forth in the opinion appear to have controlled the decision of the court—there was either an order of court or a stipulation of the parties, made during the term, extending the period within which the bill of exceptions might be settled to a time beyond the expiration of the term in which the judgment was rendered. We stated heretofore that in the *Pacific Bank* case there was such a stipulation. This fact does not appear from a reading of the opinion, however. Nevertheless, it is a fact that the court had before it such stipulation. At the time of the decision, on the Circuit Court of Appeals for the Ninth Circuit were Circuit Judges Morrow, Ross and Gilbert. This *Pacific Bank* case again came before the Circuit Court of Appeals for the Ninth Circuit in October, 1924. At that time sitting upon said court were Circuit Judges Gilbert, Ross and Hunt. The matter came up upon a writ of error to the District Court of the United States for the Southern District of California, Southern Division, in the case entitled:

*A. T. & S. F. Ry. Co. v. Nichols*, 2 F. (2d)  
12.

The following are extracts from the opinion of the court:

Counsel for defendant-in-error move to strike out the bill of exceptions upon the ground that it was not settled during the term in which the case was tried and that no extension was granted.

“Plaintiff-in-error cites the opinion of this court in *Pacific Bank v. Hannah*, 90 Fed. 72, 32 C. C. A. 522, where it was said that the bill of exceptions, having been filed within the term at which judgment was rendered, was sufficient to preserve the rights of a party presenting the bill of exceptions for allowance and settlement.

“That case is not in point, for there the findings and conclusions were filed March 24, 1897, and judgment was rendered on that day. Orders extending time to file exceptions to the findings and conclusions were made on that day and several times thereafter *during the term of court*. The bill of exceptions was filed March 28, and on June 2d a proposed amendment was filed and stipulation was had between counsel, extending time for further amendments until matters could be brought to the attention of the court. The February term was adjourned June 30, 1897, but the bill of exceptions was not signed until July, and doubtless upon the authority of *Waldron v. Waldron*, 156 U. S. 361, cited in the opinion. The signing of the bill of exceptions after the adjournment of the term at which judgment was rendered was sustained.”

We believe that the bill of exceptions was settled, signed and certified to this court in contravention of law, in that the term had expired before the same was offered for settlement, and accordingly that the motion to strike the same should be granted.



If our contention is correct that the bill of exceptions has been signed and certified to this court in contravention of law, and the motion to strike is granted, thirty of the thirty-one assignments of error will be disposed of. The first assignment of error, viz., that the amended complaint does not state a cause of action [Tr. p. 522], is the only one that may be considered without an examination of the evidence.

In the absence of a bill of exceptions, questions respecting the admissibility of evidence are excluded from consideration, and the review is confined to what appears upon the face of the pleadings and the findings.

Porto Rico v. Emmanuel, 235 U. S. 251-255;  
Rosaly v. Graham, 227 U. S. 584, 590;  
Buessel v. U. S., 258 Fed. 811, 818.

## II. ASSIGNMENTS OF ERROR.

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**Although There Are Thirty-one Assignments of Error (Brief, Pages 34-48) Relied Upon by the Plaintiff in Error in Its Brief, Only Two Questions Are Reviewable Under the Writ. They Are:**

1. *Does the amended complaint state facts sufficient to constitute a cause of action against the defendant?* and

2. *Do the facts found support the judgment?*

The first question stated being assignment of error number 1 [Tr. p. 522], raises a question of law presented to the court upon which an adverse ruling was

made and an exception was then taken. The second question stated may be raised under the writ because of the fact that the court made special findings of fact. [Tr. pp. 118 to 155.] No other question is raised by the writ for the reason that all assignments, save the second (motion for nonsuit [Tr. p. 379]), in which instance the plaintiff-in-error failed to preserve an exception to the ruling of the court, deal with the sufficiency of the evidence to support the judgment, and although the plaintiff-in-error moved the trial court to make special findings in its favor, the court was not requested to rule and did not pass upon the motion or request; neither is there any exception noted upon which an assignment of error might be predicated.

### **The Facts Involved.**

This action was tried and determined by a court without the intervention of a jury, the attorneys of record having filed with the clerk a stipulation in writing waiving a jury. [Tr. p. 116.]

The court made special findings of fact in favor of the defendant-in-error. [Tr. pp. 118-154.]

There is printed in the transcript of record [Tr. pp. 467-477] a request of plaintiff in error for special findings of fact. These special findings had been presented at a former trial of the case and by stipulation of counsel and consent of the court [Tr. p. 462] it was agreed that said special findings might be considered as refiled and the request again made. There is nothing in the record to disclose that the findings were

ever presented to or considered by the trial court. There is no ruling of the trial court upon such "Request for Special Findings of Fact"; there is no request for a ruling, and there is no exception noted to any ruling of the court upon the special findings or to the failure of the court to rule upon such request for special findings. It is apparent that counsel for plaintiff in error attached no significance to the refileing of the special findings of fact—the stipulation covering the matter having been suggested and presented by counsel for defendant in error [Tr. p. 462]—for immediately following such stipulation counsel presented orally a motion [Tr. pp. 462-466], which in effect is a request for declarations of law and special findings of fact. Upon its presentation a colloquy ensued between the trial court and counsel presenting the motion [Tr. p. 466] which discloses that the court made no ruling upon the motion or request; that counsel for plaintiff in error not only did not request a ruling upon the motion but expressed his understanding that no ruling was being made and apparently that he was satisfied with this action on the part of the court, and there is not elsewhere in the record any ruling upon this motion, any request for a ruling, or any exception preserved upon which an assignment of error might be predicated.

The plaintiff in error has assigned 31 specifications of error [Tr. pp. 522-536]. The first assignment of error specifies the overruling of a demurrer to the amended complaint [Tr. p. 522]; the record discloses an exception to the ruling [Tr. p. 59]. The second



assignment specifies the overruling of the motion for nonsuit [Tr. p. 523], the record discloses no exception to the ruling [Tr. p. 379]. Assignments numbered 3 to 26, both inclusive, assign the insufficiency or lack of evidence to support the findings of the court [Tr. pp. 523-535]. Assignments numbered 27 and 28 specify that the court erred in awarding judgment for the defendant in error and that said judgment is contrary to law and the cause made and facts stated in the pleadings and record [Tr. p. 535]. Assignment numbered 29 specifies the failure of the court to grant the request of plaintiff in error for special findings of fact [Tr. p. 535]. There was no ruling of the trial court and no exception taken [Tr. pp. 466-467]. Assignments numbered 30 and 31 specify the failure of the court to find on two particular matters therein mentioned [Tr. pp. 535, 536]. There is no exception noted in the record to support this assignment [Tr. pp. 466, 467].

There is nowhere in the brief any reference to the pages of the transcript of record showing the manner in which the error assigned arose, the ruling of the court, or the preserving of an exception; neither is there in the printed transcript of record appropriate notations *i. e.*, exception number 1, exception number 2, etc.), indicating that the matter there occurring constitutes the subject matter of an exception.

## THE LAW INVOLVED.

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### Nature and Extent of Assignments Reviewable.

Where an action is tried by the court without a jury the rulings of the court in the progress of the trial if excepted to at the time and duly presented by a bill of exceptions may be reviewed upon writ of error; when the finding is special such review may extend to the determination of the sufficiency of the facts found to support the judgment; if it is sought to test the sufficiency of the evidence to support the judgment special requests to the trial court to find the facts must be made and if the request is denied and an exception taken the denial presents a question of law.

(1) Revised Statute, Section 649.

“Issues of fact in civil cases in any Circuit Court may be tried and determined by the court, without the intervention of a jury, whenever the parties, or their attorneys of record, file with the clerk a stipulation in writing waiving a jury. The finding of the court upon the facts which may be either general or special shall have the same effect as the verdict of a jury.” Comp. St. 1918, Sec. 1587.

(2) Revised Statute, Section 700.

“When an issue of fact in any civil cause in a Circuit Court is tried and determined by the court without the intervention of a jury, according to section 649, the rulings of the court in the progress of the trial of the cause, if excepted to at the time, and duly presented by a bill of exceptions, may be reviewed by the Supreme Court upon a

writ of error or upon appeal; and when the finding is special, the review may extend to the determination of the sufficiency of the facts found to support the judgment." Comp. St. 1918, Sec. 1668.

- (3) U. S. v. Columbia and N. R. R. Co., 274 Fed. 625 (C. C. A., 9th Cir.);
- (4) Stoffregan v. Moore, 271 Fed. 680, 681.

"The fundamental rule that on writ of error only questions of law may be reviewed may serve as a guide to counsel on the trial of actions at law without a jury. The court at its discretion may make findings of fact either general or special. If they are special the question of law as to whether the special findings support the judgment may be reviewed; also the objections to the omission or exclusion of evidence during the trial. If it is sought to test the sufficiency of the evidence to support the judgment some request to the trial court to find facts or declare the law must be made, and if the requests are denied, then the denial presents a question of law. \* \* \*

There is a bill of exceptions which purports to contain the evidence taken at the trial but such bill of exceptions is not an agreed statement of the case *and it contains no ruling of the trial court upon which the assignments of error can be based.*"

- (5) Mason v. U. S. 219 Fed. 547, 549.

### Excessive Number of Assignments Condemned.

The Supreme Court and the Circuit Courts of Appeals have repeatedly condemned the practice of filing a large number of assignments. It perverts the pur-



pose sought to be subserved by the rule requiring assignments. It points to nothing and thwarts the purpose of the rule by which it was intended to present to the court a clear and concise statement of material points on which plaintiff in error intends to rely.

- (1) Ches. & Del. Canal Co., v. U. S. 250 U. S. 123, 124.

“There are forty-one assignments of error in this court which counsel in their brief compress into five questions and these resolve themselves at once into three \* \* \*. Such a record constrains us to repeat the following:

‘This practice of unlimited assignments is a perversion of the rule, defeating all its purposes, bewildering the counsel of the other side, and leaving the court to gather from a brief, often as prolix as the assignments of error, which of the latter are really relied on.’”

- (2) Central Vermont Ry. Co. v. White, 238 U. S. 507, 509;
- (3) Phillips etc. Construction Co. v. Seymour, 91 U. S. 646, 648.

“The object of the rule requiring an assignment of errors is to enable the court and opposing counsel to see on what points the plaintiff’s counsel intend to ask a reversal of the judgment, and to limit the discussion to those points. This practice of unlimited assignments is a perversion of the rule, defeating all its purposes, bewildering the counsel of the other side, and leaving the court to gather from a brief, often as prolix as the assignments of error, which of the latter are

really relied on. We can only try to respond to such points made by counsel as seem to be material to the judgment which we must render."

(4) *Fitter v. U. S.* 258, Fed. 567, 569;

(5) *Clark v. U. S.* 258 Fed. 437 at 438.

### **Necessity for Obtaining a Ruling and Noting an Exception.**

Whether there is any substantial evidence to sustain a finding is reveiwable as a question of law only when a request or motion is (1) *made*, (2) *denied*, and (3) *excepted to*, or some other like action is taken which *fairly presents* that question to the trial court *and secures its ruling thereon* during the trial

(1) *Wear v. Imperial Window Glass Co.*, 224 Fed. 60, 63;

(2) *Mercantile Trust Company v. Wood*, 60 Fed. 346, 348.

"The special finding referred to in this conclusion is not a report of the evidence, but it must be, like the special verdict of a jury, a finding of the ultimate facts which the evidence establishes. The only question the special finding presens that would not be presented by a general finding is whether or not, in any view, the facts found in it are sufficient to support the judgment. With the single exception of this question, which is presented by the special finding itself, there are only two methods by which questions of law can be so presented to the court that tries the facts that this court can review them by writ or error. These methods are, first, by seasonable objections

and exceptions to the rulings of the court upon the admission or rejection of evidence, and, second, by requesting the court before the trial is ended, to make declarations of law, and *excepting to its refusal* to do so, and to its declarations of law, *if any*, that *do not accord with the propositions asked*, in exactly the same way as instructions to a jury would be requested, and the rulings of the court giving or refusing them would be excepted to, if the trial was before a jury. The finding of the court, whether general or special, performs the office of a verdict of a jury. When it is made and filed, the trial is ended. Exceptions to the finding, or to statements of legal conclusions contained in it, or in an opinion in which it is contained, or in an opinion filed with it, avail nothing. They are as futile as exceptions to the verdict of a jury. When a case comes to this court upon a writ of error, this is a court for the correction of the errors of the court below solely. To enable us to review those errors in a case tried by the court it must appear that the legal propositions on which they rest were presented to that court *and ruled upon* before the trial ended, unless they are involved in the single question whether or not the facts found in a special finding are sufficient to support the judgment. It is, in the words of the statute, 'the rulings of the court in the progress of the trial of the case,' and these only, that we are authorized to review, unless such rulings are involved in the single question we have mentioned. (Citing cases)."

- (3) *Seep v. Ferris-Haggarty etc. Co.*, 201 Fed. 893, 895;



- (4) *Pennsylvania Casualty Co. v. White Way* (C. A. 9th Cir.), 210 F. 782, 784.

“When an action at law is tried before a jury, their verdict is not subject to review unless there is absence of substantial evidence to sustain it, and even then it is not reviewable unless a request has been made for a peremptory instruction and *an exception taken* to the ruling of the court. When a jury is waived, and the case is tried by the court, the general finding of the court for one or the other of the parties stands as the verdict of the jury, and may not be reviewed in an appellate court unless a lack of evidence to sustain the finding has been suggested by a request for a ruling thereon, or a motion for judgment, or some motion to present to the court the issue of law so involved, before the close of the trial. (Citing cases.)”

### **Exceptions of No Avail Unless Taken at the Trial.**

An exception must show that it was taken and preserved at the trial and this must appear affirmatively on the record. No bill of exceptions can be entertained by the Appellate Court unless it appears from the record that an exception was taken to the ruling of the court below.

- (1) *U. S. v. Carey*, 110 U. S. 51, 52;  
(2) *Mound Coal Co. v. Jeffrey Mfg. Co.*, 233 Fed. 913, 918.

### **Assignments Must Be Specific.**

General assignments of error will not be entertained.

- (1) "Rule XI. Assignment of errors. The plaintiff in error or appellant shall file with the clerk of the court below, with his petition for the writ of error or appeal, any assignment of errors, which shall set out separately and particularly each error asserted and intended to be urged."
- (2) *Guerini Stone Co. v. Carlin Construction Co.*, 248 U. S. 334, 348;
- (3) *U. S. v. U. S. F. & G. Co.*, 236 U. S. 512, 529;
- (4) *McDermott v. Severe*, 202 U. S. 600, 610;
- (5) *Bank of Italy v. Roneo & Co.* (C. C. A. 9th Cir.), 287 Fed. 5, 8;
- (6) *Grape Creek Coal Co. v. Farmers' Loan & Trust Co.*, 63 Fed. 891, 894.

"The second and third specifications of error do not, in conformity with the eleventh rule of this court, 'set out separately and particularly' the error intended to be urged. An assignment cannot be good, under this rule, if it is necessary to look beyond its terms, to the brief, for a specific statement of the question sought to be presented."

- (7) The "Francis Wright", 105 U. S. 381, 389.

"There is another equally fatal objection to this bill of exceptions. An evident effort has been made here, as it has been before, to so frame the exceptions as, if possible, to secure a re-examination of the facts in this court. The transcript which has been sent up contains the pleadings and all the testimony used on the trial below. The bill of exceptions sets forth that at the trial the pleadings were read by the respective parties, and the testimony then put in on both

sides. This being done, the libellants presented to the court certain requests for findings of fact and of law. These requests were numbered consecutively, sixteen relating to facts and three to the law. Afterwards, six additional requests for findings of fact were presented. It is then stated that the court made its findings of fact and of law and filed them with the clerk, together with an opinion in writing of the circuit justice who heard the cause. The libellants then filed what are termed exceptions to the findings and the refusals to find. In this way exceptions were taken separately to each and every one of the facts found and the conclusions of law, and to the refusal to find in accordance with each and every one of the requests made. The grounds of the exceptions are not stated. Many of the requests of the libellants are covered explicitly by the findings as actually made, some being granted and others refused.

“We have no hesitation in saying that this is not a proper way of preparing a bill of exceptions to present to this court for review rulings of the Circuit Court such as are now complained of. A bill of exceptions must be ‘prepared as in actions at law’, where it is used, ‘not to draw the whole matter into examination again’, but only separate and distinct points, and those of law.”

- (8) *Wear v. Imperial Window Glass Co.*, 224 Fed. 60, 63.

“The only question the specifications of error attempt to present is whether or not the evidence, which is conflicting, sustains the finding and judgment of the court. They invite this court, in other words, to retry this case and to determine whether or not under the applicable law the



weight of the evidence sustains the finding and judgment. But the case was tried by the court below without a jury, and its decision of that issue is not reviewable in this court. It is, like the verdict of a jury, assailable only on the ground that there was no substantial evidence in support of it, and then it is reviewable only when a request has been made to the trial court before the close of the trial that it adjudge, on the specific ground that there was no substantial evidence to sustain any other conclusion, either all the issues or some specific issue in favor of the requesting party. No such request was made in this case, and the specifications of error, therefore, present no question reviewable by this court. When an action at law is tried without a jury by a federal court, and it makes a general finding, or a special finding of facts, the act of Congress forbids a reversal by the appellate court of that finding, or the judgment thereon, 'for any error of fact' (Revised Statutes, Sec. 1011 [U. S. Comp. Stat. 1913, Sec. 1672, p. 700]), and a finding of fact contrary to the weight of the evidence is an error of fact.

"The question of law whether or not there was any substantial evidence to sustain any such finding is reviewable, as in a trial by jury, only when a request or a motion is made, denied, and *excepted to*, or some other like action is taken which fairly presents that question to the trial court and *secures its ruling thereon* during the trial. (Citing cases)."

### The Object and Purpose of an Exception.

The sole purpose of a bill of exception and assignment of errors is to bring the matters complained of

separately and clearly (1) before the trial judge so that he may have the opportunity to grant relief if he thinks proper, (2) before counsel for defendant in error, so that he may be advised of the precise points to be made in argument, and (3) before the appellate court, so that it may readily perceive the points to be decided and the portions of the record on which they depend.

- (1) *Fillippon v. Albion Vein Sale Co.*, 250 U. S. 76, 82.

“\* \* \* the primary and essential function of an exception is to direct the mind of the trial judge to the point in which it is supposed that he has erred in law, so that he may reconsider it and change his ruling if convinced of error, and that injustice and mis-trials due to inadvertent errors may be obviated.”

- (2) *Guerini Stone Co. v. Carlin Construction Co.*, 248 U. S. 334 at 338;

- (3) *U. S. v. U. S. F. & G. Co.*, 236 U. S. 512 at 529.

“An exception therefore furnishes no basis for reversal upon any ground other than the one specifically called to the attention of the trial court.”

- (4) *Robinson & Co. v. Belt*, 187 U. S. 41, 50.

“While it is the duty of this court to review the action of subordinate courts, justice to those courts requires that their alleged errors should be called directly to their attention, and that their action should not be reversed upon questions which the astuteness of counsel in this court has evolved from the record.”

(5) Buessel v. U. S. 258 Fed. 811, 819.

“In Michigan Insurance Bank v. Eldred, 143 U. S. 293, 298 \* \* \*, Mr. Justice Gray stated the rule and declared that by the uniform course of decision no exceptions to ruling could be considered, unless they were taken at the trial and were also embodied in a formal bill of exceptions \* \* \*. The court held, therefore, that an exception furnishes no basis for reversal upon any ground other than the one *specifically* called to the attention of the trial court.”

Bearing in mind the principles announced and the practices prescribed by the authorities just cited, we draw the following conclusions respecting plaintiff in error's thirty-one assignments of error.

1. Assignment number 1 [Tr. p. 522]—overruling demurrer to the amended complaint—may be reviewed, being an adverse ruling upon a question of law, an exception having been preserved. [Tr. p. 59.]

2. Assignment number 2 [Tr. p. 523]—denying motion for non-suit—may not be reviewed, no exception having been taken at the time to the ruling of the court. [Tr. p. 379.]

3. Assignments numbered 3 to 31, both inclusive, may not, neither may any of them be reviewed because of the failure of the plaintiff in error during the trial to present a request or motion submitting the matters therein specified for the court's consideration, obtaining a ruling thereon and preserving an exception to such ruling.

4. Assignments numbered 3 to 26, inclusive [Tr. 523-535], specify the alleged insufficiency of the evi-



dence to sustain the findings. Of these twenty-four assignments the following, towit: numbers 3, 5, 8, 9, 10, 11, 12, 15, 16, 17, 18, 19, 21, 22, 23, 24, 25 and 26, may not be considered for the reason that they do not conform with Rule 11 of this court. They are not specific and in order to obtain a specific statement of the question sought to be presented, it is necessary to look beyond the terms of the assignment to the brief of the plaintiff in error.

5. Assignments numbered 27 and 28, assigning generally as error the finding for the defendant in error and against the plaintiff in error, and assignments numbered 30 and 31, specifying the failure of the court to find in certain particulars therein specified are subject to the same criticism as those assignments specified in the immediately preceding paragraph number 3, namely, they do not comply with Rule 11 of the court; they are not specific and it is necessary to examine the brief of the plaintiff in error to obtain a specific statement of the question sought to be presented.

6. Assignment number 29 specifying the refusal of the court to make findings in accordance with "request for special findings of fact" of plaintiff in error may not be assigned for the reason that the special findings were not actually and fairly presented to the court for ruling; were not passed upon by the court, and no exception to the ruling or failure of the court to rule was preserved.

The failure of the plaintiff in error to obtain a ruling upon its oral motion for declarations of law and special findings [Tr. p. 466] or to call to the attention of the court and obtain a ruling upon its written special findings with the accompanying absence of any exceptions taken and preserved during the course of the trial, limits the review of this court under the writ to the questions:

1. *Does the Amended Complaint State Facts Sufficient to Constitute a Cause of Action Against the Defendant?* and
2. *Do the Facts Found Support the Judgment?*

### III. SEVEN POINTS OF PLAINTIFF IN ERROR.

Plaintiff in error, as we believe, in disregard of the rules and practice of this court, as outlined in the preceding subdivision of this argument, after having filed an omnibus assignment of errors consisting of 31 separate specifications, arranges the assignments into seven groups setting forth for each group his deduction of the point raised by the various assignments in that particular group. These seven contentions have been by counsel for plaintiff in error arranged under seven general headings (Br. pp. 49-52) and thereafter in consecutive order have been presented for the court's consideration (Br. pp. 53-139). We shall undertake a consideration of these seven "Points of Plaintiff in Error" in the order of their announcement.

**Points of Plaintiff in Error Numbers I and II  
Answered.**

The assignments of error numbers 1, 2, 3, 15, 22, 27, 28 and 29 are by plaintiff in error grouped under two headings, namely:

(I) "The Cotton Company sustained no loss by reason of the alleged acts of J. B. Sears, its secretary, in wrongfully converting or wilfully misapplying the 1091 warehouse tickets or the cotton represented thereby, and which were covered by unredeemed trust receipts held by plaintiff bank, and the court erred in finding that any such loss was incurred by the Cotton Company;" and

(II) "The first cause of action in plaintiff's complaint as amended does not state facts sufficient to constitute a cause of action against defendant Bonding Company, and the trial court erred in overruling defendant's demurrer thereto and in refusing to find judgment for the defendants."

An examination of the eight specific assignments grouped under these two "Points" and the argument of counsel in support thereof (Br. pp. 53-74) disclose that the contention made by plaintiff in error is:

"That a cause of action was not pleaded; that the facts found did not sustain the judgment; that the evidence does not sustain the judgment, and that the judgment is against the law and the facts of the case."

Because the two questions which we concede may be urged under the writ are here involved in their entirety, the two points of the plaintiff in error have been discussed at greater length than might otherwise be justified.



### The Facts Involved Under Points I and II.

The alleged insufficiency of the pleadings and proof, as we conclude from an analysis of the argument of plaintiff in error (Br., pp. 53-73), is ascribed to the fact that the proceeds of the 1091 bales of cotton, disposed of by Sears in violation of the terms of the trust agreement and misapplied to the payment of losses incurred by him in the transaction of the business of the Cotton Company instead of in the redemption of the trust receipts, fails to indicate any loss of money or personal property of the Cotton Company including that for which it may be responsible to others.

The court found, and the correctness of the findings are not challenged, that between November 19, 1920, and April 25, 1921, Sears, with the intent then and there entertained by him of dishonestly misappropriating and wilfully misapplying the warehouse receipts, the cotton represented thereby and the proceeds obtained therefrom, and with the fraudulent intent of causing a loss to the Cotton Company of its money and personal property for which it would be and has become responsible to the plaintiff Bank, applied to and secured from the plaintiff Bank the warehouse receipts then in its possession [Finding No. 6, Tr. p. 128]; and as a part of said transaction delivered the trust receipts in question [Tr. p. 129], explaining the necessity for the surrender of the receipts in order to make sales of the cotton, promising upon the exchange of the warehouse receipts for bills of lading to return the bills of lading and take up the warehouse receipts [Tr. p. 130].

That during this time and pursuant to said fraudulent and dishonest plan and scheme entertained by him, Sears surrendered the warehouse receipts obtained from the plaintiff Bank, sold the cotton represented thereby and received from the common carriers bills of lading therefor, and immediately thereafter, in violation of his promises and representations to the plaintiff Bank and in violation of the terms of the trust receipts, but pursuant to the dishonest plan and scheme entertained by him, Sears prepared sight drafts upon the parties to whom he had sold the cotton, attached the bills of lading thereto, and thereupon presented the sight draft, bill of lading attached, to an officer of the plaintiff Bank other than the officer from whom Sears had obtained the warehouse receipts and to whom he had delivered the trust receipts, and represented to such officer to whom the sight drafts were presented that the cotton covered by said sight drafts and bills of lading was cotton belonging to the Cotton Company and wilfully failed to disclose to said officer that the plaintiff Bank then held trust receipts of the Cotton Company given by said Sears covering said cotton described in said bills of lading attached to said sight drafts [Finding No. 7, Tr. pp. 131-132]. That having secured the approval of said officer (which authorized the teller to accept the sight draft as a cash deposit and not for collection [Tr. p. 133], Sears deposited the sight draft and bill of lading and secured a cash credit entry) upon the bank pass book of the Cotton Company, in the amount of the sight draft, and immediately thereafter, pursuant to his fraudulent

scheme, falsified the books of the Cotton Company by entering therein the various amounts of the sight drafts and carrying these upon the books of the Cotton Company as credit items without limitation of any kind and wilfully failed to enter any memorandum or book entry showing that the warehouse receipts had been secured by the issuance of trust receipts, or that trust receipts had been issued, or that moneys and credits entered in the bank pass book were received by the sale of cotton covered by trust receipts held by the bank, and failed to make any entry indicating that the money shown in the cash account was other than absolute and unencumbered funds of the Cotton Company [Tr. pp. 133-134]. That Sears, pursuant to his fraudulent and dishonest plan and scheme, during said time represented to the officers and directors of the Cotton Company that the various sums of money and credits entered upon the bank pass book and the books of account of the Cotton Company were moneys of said Cotton Company made and accumulated by Sears in the conduct of its affairs, and upon inquiry made of him represented to the officers of the plaintiff Bank that the Cotton Company still retained, and that he as its secretary still had in his custody in the vaults of the Cotton Company, all the warehouse receipts surrendered to him by the plaintiff Bank [Tr. pp. 134-135]. That the directors and officers of the Cotton Company and of the plaintiff Bank believed, acted upon and were deceived by the dishonest and fraudulent representations and statements of Sears [Tr. p. 135].



That Sears, pursuant to his fraudulent and dishonest plan and scheme, and contemporaneously with the several fraudulent and dishonest conversions and misapplications of the warehouse receipts and cotton represented thereby and the moneys and credits realized therefrom, and pursuant to the false and fraudulent representations made and deceits practiced by Sears upon the Cotton Company and the plaintiff Bank, Sears, continuing to act as secretary of the Cotton Company, fraudulently and dishonestly misappropriated and wilfully misapplied the moneys and funds placed to the credit of the Cotton Company following the various dishonest and fraudulent sales of cotton and disposition of warehouse receipts as hereinbefore mentioned by using said moneys and funds for the purpose of dealing and speculating in cotton in the name of the Cotton Company, conducting such speculations at a loss and paying said losses out of said moneys and funds, and in the payment of claims and demands incurred by Sears in such dealings and speculations in cotton [Finding No. 8, Tr. pp. 135-136]. That relying entirely upon the false and fraudulent representations of Sears as herein mentioned and the deceits practiced by him upon them, the directors and officers of the Cotton Company continued the business of the Cotton Company and consented to Sears, subsequent to the 19th day of November, 1920, continuing to act as secretary of said Cotton Company and to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith upon its behalf. That said Cotton Company, its directors

and officers, would not have consented to the continuing of the business of the Cotton Company subsequent to the 19th day of November, 1920, neither would they have consented to Sears continuing to act as secretary after said date, neither would they subsequent to said date have consented to Sears conducting any dealings or speculations in cotton nor incurring any indebtedness or contracting any financial obligations upon its behalf had it or its directors or officers, other than said Sears, known of the frauds and deceits, or any of them, being practiced upon said Cotton Company and said plaintiff Bank by said Sears as hereinbefore mentioned [Tr. pp. 137-138]. That because of the frauds, deceits and dishonesty so perpetrated by Sears, said Cotton Company has sustained a loss and has become and is responsible to the plaintiff Bank in an amount in excess of the penalties of the bond [Finding No. 9, Tr. p. 138].

### **The Law Involved Under Points I and II. Construction of Terms of Bond.**

(a) Fidelity bonds of a surety company are construed most strongly against the surety and in favor of the indemnity, and wherever a bond is fairly open to two constructions, one of which will uphold and the other defeat the claim of the insured, that which is the more favorable to the insured will be adopted.

#### **1. 21 R. C. L. p. 1160, Sec. 200.**

“200. Measure of Liability.—The law of suretyship has undergone a considerable change in late years. The day of personal suretyship is fast

slipping away, and in its stead comes the corporate surety for profit. Formerly, a surety was an individual, or collection of individuals, actuated by beneficent motives to carry the burden of the suretyship, receiving no profit or benefit, and, in consequence thereof, the law dealt tenderly with him or them. But, in this day and age of corporate sureties, the burden is lightened by the payment of adequate premiums, and their final liabilities are oft-times secured by counter indemnity. As a result of this new condition of affairs the trend of all modern decisions, federal and state, in the construction of the law appertaining to sureties is to distinguish between individual and corporate suretyship, where the latter is an undertaking for money consideration by a company chartered for the conduct of such business. In the one case, the rule of *strictissimi juris* prevails as it always has, that is, the contract of an individual surety, or a 'voluntary surety' as he is spoken of in some cases, will be strictly construed and all doubts and technicalities resolved in favor of the surety, such person being regarded as a favorite of the law. But in the other case, because *it is essentially an insurance against risk*, underwritten for a money consideration by a corporation adopting such business for its own profit, the contract will be construed most strongly against the surety and in favor of the indemnity which the obligee has reasonable grounds to expect. And, in general, as the contracts of surety companies are essentially contracts of indemnity, the courts ordinarily apply to them by analogy the rules of construction *applicable to contracts of insurance*. Hence, *in an action on a bond written*



by a surety company, if the bond is fairly open to two constructions, one of which will uphold and the other defeat the claim of the insured, that which is most favorable to the insured will be adopted. Moreover, the courts generally hold that such a company can be relieved from the obligation for suretyship only where a departure from the contract is shown to be a material variance, or, as it has been otherwise expressively stated, the modern day surety company must show some injury done before it can be absolved from the contracts which it clamors to execute. For, it has been said, to allow such companies to collect and retain premiums for their services, graded according to the nature and extent of the risk, and then to repudiate their obligations on slight pretexts that have no relation to the risk, would be most unjust and immoral and would be a perversion of the wise and just rules designed for the protection of voluntary sureties."

2. 32 Cyc. p. 306, par. E;

3. Amer. Surety Company v. Pauly, 170 U. S. 133.

"If, looking at all its provisions, the bond is fairly and reasonably susceptible of two constructions, one favorable to the bank and the other favorable to the surety company, *the former*, if consistent with the objects for which the bond was given, *must be adopted*, and this, for the reason that the instrument which the court is invited to interpret was *drawn by the attorneys*, officers, or agents of the surety company. This is a well established rule of the law of insurance. National Bank v. Insurance Co., 95 U. S. 673; Western Ins. Co. v. Cropper, 32 Penn. St. 351, 355;

Reynolds v. Commerce Fire Ins. Co., 47 N. Y. 597, 604; Travelers' Ins. Co. v. McConkey, 127 U. S. 661, 666; Fowkes v. Manchester etc. Life Ass'n., 3 Best & Smith, 917, 925. As said by Lord St. Leonards in Anerson v. Fitzgerald, 4 H. L. Cas. \*484, \*507, 'it (a life policy) is of course prepared by the company, and if therefore there should be any *ambiguity* in it, must be taken, according to law, *most strongly against the person who prepared it.*' There is no sound reason why this rule should not be applied in the present case. The object of the bond in suit was to indemnify or insure the bank against loss arising from any act of fraud or dishonesty on the part of O'Brien in connection with his duties as cashier, or with the duties to which in the employer's service he might be subsequently appointed. *That object should not be defeated by any narrow interpretation of its provisions, nor by adopting a construction favorable to the company if there be another construction equally admissible under the terms of the instrument executed for the protection of the bank.*" (p. 144.)

4. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Fed. p. 353 (Circuit Court of Appeals, 8th Circuit);
5. Champion I. M. & C. S. Co. v. American Bonding & Trust Co., 115 Ky. 863, 75 S. W. 197.

"It will be observed that the bond in this case is a *printed one*—prepared, doubtless, by a skilled attorney in appellees' employ. The contract expressed therein is but a *form of insurance*, and the law of insurance is that, in the construction of policies, if there be any *ambiguity* in them, it must

be considered *most strongly against the insurance company*. In *American Surety Company v. Pauly*, 170 U. S. 133, 18 Sup. Ct. 552, 42 L. Ed. 977, Mr. Justice Harlan admirably states this rule." (p. 198.)

6. *Remington v. Fidelity & Deposit Company of Maryland*, 27 Wash. 429, 67 Pac. 989.

"The provisions in the contract above quoted are for the protection of the insurance company. They were not intended to avoid an existing liability under the contract or as a means of defeating recovery thereon, but *only to prevent further liability* after discovery of dishonesty by the employer. *For such purpose, the provisions are reasonable and will be maintained, but if they are to be considered as a shield to avoid a liability legally and rightfully due, or to avoid a contract properly made, they are a fraud upon the rights of the insured, and cannot be upheld.* The words 'The employer shall immediately give notice to the company' should receive such interpretation as not to fritter away the substantial rights of the parties, nullify the contract, or promote fraud." (pp. 991-2.)

7. *Title Guaranty & Surety Company v. Bank of Fulton*, 89 Ark. 471, 117 S. W. 537.

"In order to determine whether these statements are warranties or mere representations, it is necessary to consider the nature of the bond sued on and what construction the law makes relative to the provisions of such bonds. This is not an ordinary obligation given by a surety, but it is an indemnity bond and is in the nature of a *contract of insurance, insuring the fidelity of the employee.*



It is said by this court in *American Bonding Co. v. Morrow*, 80 Ark. 49, 96 S. W. 613: 'It is now well settled that the bond of a surety company, like any other insurance policy, is to be *most strongly construed against the insurer*. The language of the bond is that *selected and employed by the insurer*, and when doubtful or *ambiguous must be given the strongest interpretation against the insurer which it will reasonably bear*.' And so in determining the nature of the provisions of this bond, we first look to see whether the provisions are susceptible of two constructions. If they are, then *we must adopt that construction which is most favorable to the bank*. This is the well settled doctrine as to the construction of such instruments as the bond sued on in this case. *American Surety Co. v. Pauly*, 170 U. S. 133." (p. 540.)

(b) The dishonesty covered by the bond of fidelity insurance need not be acts constituting a crime and punishable as such.

1. *United States v. Northway*, 120 U. S. 327.

"The offense of wilfully misapplying the funds of a banking association, as defined by the statute, was considered with reference to the facts in that case. It was there held that a wilful and criminal misapplication of the funds as defined by Sec. 5209, *did not include every case of an unlawful application of funds*, inasmuch as in the very statute itself there were other instances of unlawful misapplication evidently not embraced within the intention of Sec. 5209. For that reason it was held, in that case, that it was necessary to specify the particulars of the application, *so as to distin-*

*guish that charged in the indictment as wilful and criminal from those others contemplated by the statute which are unlawful but not criminal.”*  
(p. 332.)

2. Citizens Trust and Guarantee Company v. G. & R. F. Insurance Company, 229 Federal, 326 (Circuit Court of Appeals, 4th Circuit);
3. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Federal, 353 (C. C. A., 8th Circuit);
4. City Trust Company v. Lee, 204 Ill. 69, 68 N. E. 485;
5. Rankin v. U. S. F. & G. Co., 99 N. E. 314, 86 Ohio St. 267.

(c) To justify a recovery under a bond indemnifying an employer against loss by reason of the fraud or dishonesty of an employee, it is not necessary to show that the acts complained of resulted in profit to, or were calculated or intended to result in profit to, the employee.

1. U. S. F. & G. Co. v. Egg Shippers F. & S. Co., 148 Fed. 353 (C. C. A., 8th Circuit).

“The test is not whether he intended to personally profit by his course, though that he did is perhaps a permissible inference from the facts shown. He occupied a position of trust and confidence which he secretly betrayed. He received compensation for guarding the interests of his employer and he was wilfully, intentionally and grossly faithless. *This is not a case of mere indiscretion or error of judgment. There was a breach of trust, a want of financial integrity*

*coupled with deceit and concealment, and resulting in financial loss to the employer. This was both fraud and dishonesty within the meaning of the bond. Cases involving fidelity bonds insuring against 'embezzlement and larceny' or 'fraud and dishonesty amounting to embezzlement or larceny' are obviously not in point."* (148 Fed. 355.)

2. Rankin v. U. S. F. & G. Co., 99 N. E. 314, 86 Ohio St. 267;
3. Roseville Trust Company v. American Surety of New York, 91 N. J. Law 558, 103 Atlantic 182

(d) By the term "wilfully" is meant purposely or designedly. The intent to injure and defraud, which is necessary to constitute a wilful misapplication, does not necessarily involve any malice or ill will but merely that general intent to injure and defraud which always arises in contemplation of law when one wilfully and intentionally does that which is illegal or fraudulent and which in its necessary and natural consequences must injure another.

1. Agnew v. United States, 165 U. S. 36;
2. Walsh v. United States, 174 Federal 615 (C. C. A.);
3. Pearce v. United States, 192 Federal, 561 (C. C. A.).

(e) Where a clause of the bond is being construed all the language and not merely a portion thereof must be taken into consideration.

1. Kansas Flour Mills Company v. American Surety Company, 98 Kansas 587, 158 Pac. 1118;



2. Campbell v. Maryland Casualty Co., 52 Ind. App. 228, 97 N. E. 1026.

(f) To constitute a wilful misapplication even in criminal cases it is only necessary to show the acts complained of were performed purposely and designedly.

1. Pearce v. United States, 192 Fed. 561 (C. C. A.)

### Discussion.

1. Under the terms of the bond, the Maryland Casualty Company agreed that it would

“reimburse the employer for any loss \* \* \* of money, securities or other personal property (including that for which the employer may be responsible to others) which the employer shall have sustained by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication on the part of the employee while in the performance of his duties as secretary. \* \* \*”

Excluding from consideration the parenthetical phrase, it is our contention that the Cotton Company has sustained a *loss* within the restricted and technical meaning of the word in this: that securities—cotton tickets—to the number of 1091 have been lost to the Cotton Company through Sears’ lack of fidelity. The loss is shown by the following facts: The cotton was purchased and paid for by the Cotton Company. The money was furnished by the bank in the nature of a loan upon acceptances secured by cotton represented by warehouse tickets. Had Sears been faithful to his trust, the cotton tickets on May 1, 1921, would have

been in Sears' possession or on deposit with the Citizens National Bank, attached to the 87 acceptances, *or* they would have been exchanged for bills of lading and the bills of lading would have been in the possession of the Citizens National Bank, *or* the bills of lading having been returned to the Citizens National Bank and the trust receipts taken up, pursuant to Sears' agreement and the terms of the trust receipt, the Citizens National Bank would have forwarded sight drafts, bills of lading attached and received the money upon the delivery of the cotton, applied the same to the acceptance account and in this way there would have been no loss of cotton tickets. In other words, had Sears dealt honestly with the Cotton Company and the bank he could not have disposed of the 1091 bales of cotton to which the Bank and Cotton Company looked as security for the acceptance account. Due to Sears' perfidy, the Cotton Company has lost its cotton and the bank has lost its security.

Counsel for plaintiff in error contends, however, that inasmuch as the proceeds from the wrongful disposition of the cotton was credited to the Cotton Company on its books and upon the books of the bank, and inasmuch as the money was thereafter expended by Sears in the business of the Cotton Company (overdraft eliminated), the Cotton Company has sustained no loss. (Brief pp. 55, 56, *et seq.*)

The answer to this suggestion is that the evidence discloses that the indebtedness of the Cotton Company which was paid by Sears from the funds realized from the wrongful disposition of the cotton was indebted-

ness which would not, and could not have been incurred had he been faithful to his trust. This is not a case where the Company has two enforceable claims to meet and the employee applies funds intended for the satisfaction of one claim to the satisfaction of the other; this is an instance where the company has one enforceable claim to meet and has sufficient collateral deposited to insure the payment thereof and the employee practicing a series of frauds and deceptions incurs in the name of the company (he having the power so to do), another claim against the company (which could not have been incurred but for his duplicity) and fraudulently obtains and disposes of the collateral and uses the funds realized therefrom to extinguish the liability by him fraudulently incurred.

Coming now to a consideration of the parenthetical phrase, towit, "including that for which the employer may be responsible to others" [Tr. p. 205]. It is elementary that in the construction of any form of contract the courts will consider that language used was intended for a purpose and will not presume that the language was intended to be meaningless, or was inserted without reason therefor. In *Maryland Casualty Company etc. v. Bank of England*, 2 Fed. (2d) 793, at 795, 796, cited by plaintiff-in-error on another point (Br. p. 111), the court said: "Other rules of construction are that all parts of a contract must be given a reasonable meaning and vitality, and that parties are presumed not to insert idle, foolish, meaningless language." The language in question (parenthetical phrase) is inserted in the most important



sentence of the bond, and the courts will not conclude that it was inserted inadvertently and without the intention of including that which otherwise would not be included. We feel that it would be difficult to use language more clear or concise than that set forth in the parenthetical phrase in order to extend the scope of the term "loss of personal property" to circumstances where the fraud of employees imposed a responsibility upon the employer.

In a South Dakota case (*Farmers & Merchants Bank v. U. S. F. & G. Co.*, 28 S. D. 315, 133 N. W. 277 (37 L. R. A. [N. S.] 1153), *afterward overruled upon another point* (manipulation of stock), the court announced the proposition we declare elementary as follows:

"It must be presumed that the clause was designed to effect the rights of the parties under the contract; to either enlarge or restrict the defendant's liability as defined by the general terms of its undertaking."

The case of *Campbell v. Maryland Casualty Company*, 52 Ind. App. 228, 97 N. E. 1026, is decidedly applicable to the question under discussion. The action was instituted to recover on an employer's liability policy of insurance issued to a stone company; later, with the consent of the obligor, consigned to a second stone company. The action is by the receiver of the second stone company. A judgment was obtained against the assignee by an employee, personal injury having been received by him in the line of his employment. Before the judgment in the

personal injury action was affirmed on appeal, the assignee stone company became insolvent and passed into the hands of a receiver. The policy of insurance provided that the—

“obligor agrees to indemnify the assured \* \* \* against loss \* \* \* on account of bodily injuries \* \* \* suffered by an employee of the assured while on duty caused by the negligence of the assured.”

On the reverse side of the policy, the following provision was printed:

“8. *No action shall lie against the company as respects any loss under this policy unless it shall be brought by the assured himself to reimburse him for loss actually sustained and paid by him in satisfaction of a judgment after trial on the issue.*”

Respecting this provision, the court said:

“The language quoted from the body of the policy, as well as the language of the provision No. 8 heretofore set out, would seem to indicate that the purpose of the contract was to indemnify the assured against loss and not to protect it against liability.”

Discussing the same matter, the court states:

“If the policy sued on is a contract to indemnify against loss, it is necessary to show a damage before there can be a recovery (citing cases). *On the other hand*, if the policy sued on is a contract to protect the assured against liability merely, an action may be brought and a recovery had as

*soon as the liability is legally imposed, regardless of the question as to whether or not any actual loss or damage has been suffered (citing cases). The distinction observed between contracts to indemnify against loss and contracts to protect the assured against liability is recognized by practically all the cases cited.” (Page 1027.)*

Attached to this policy was a slip or rider which contained the following provision:

“This policy shall only cover losses sustained by and liability for any claims against the assured as a result of the risk specified in the contract  
\* \* \*.”

Concerning this language of the rider, the court said:

“This slip seems to have the effect to so *modify* the body of the policy and condition No. 8 as to make the policy cover not only losses sustained by the assured, but *also liabilities* for any claims against the assured. If the language of the slip is to be given any meaning at all, it must have the effect stated; *and it certainly will not be presumed* that the parties took the trouble to attach a slip to the policy *without intending* thereby to *change its effect*. By virtue of the slip, the policy sued on was made to cover liabilities against the assured as well as losses. The plaintiff may recover upon this policy under the authority of the cases cited without showing an actual loss. It is sufficient if he show that a liability has become legally fixed.”



This case also announces the rule we have heretofore styled as elementary in the construction of fidelity bonds to the effect that a parenthetical clause must be presumed to have been intended for some purpose and not idly nor meaninglessly inserted. The court declares:

“If the contract in question were to be construed solely from a consideration of the provisions heretofore referred to and in the light of the authorities cited, we should have no doubt as to its meaning; but the policy in this case carries a slip or rider, which, to the mind of the court, materially affects its meaning. \* \* \* *In attaching this slip to the policy, the parties no doubt intended to modify in some manner the force and effect of the language of the policy.* \* \* \* If the language of the slip is to be given any meaning at all, it must have the effect stated; and it certainly will not be presumed that the parties took the trouble to attach a slip to the policy without intending thereby to change its effect.” (p. 1028.)

An Oregon case cited in the opinion of the Indiana court, towit, *Fenton v. Fidelity & Casualty Co. of N. Y.*, 36 Ore. 283, 56 Pac. 1096, is to the same general effect as the Indiana case. The Oregon court applies *to the interpretation of the provision of the policy covering loss or liability*, the rule we have so frequently referred to:

“If, however, the meaning of the policy is in doubt, and its language is fairly and reasonably susceptible of two constructions, one favorable to the assured, and the other to the defendant, the

one is to be adopted which is the most favorable to the assured. This is the universal ruling in the construction of insurance policies, because they are drawn by the attorneys, officers, and agents of the company; and it is but fair that, if there should be any ambiguity or uncertainty in the language used, it should be construed most strongly against the company." (56 Pac. p. 1098.)

The Cotton Company, because of Sears' lack of fidelity sustained a loss of personal property consisting of 1091 bales of cotton and by reason thereof has become responsible to the Citizens National Bank in an amount in excess of the defendant's liability under the terms of the bond. What would have occurred had Sears been faithful to his trust is in many respects a matter of conjecture. What has resulted from his faithlessness is disclosed by the testimony. The testimony discloses that, had the directors of the corporation known on November 19, 1920, of Sears' fraudulent scheme to carry on the business, the consummation of the plan would have been prevented.

Plaintiff in error at page 56 of its brief submits a hypothetical case which it alleges is analogous to the case now before the court. We submit that there is entirely lacking in the illustration of plaintiff in error the controlling factor in the case now before the court. If Sears' transactions had stopped after the sale of the cotton and the deposit of the sight draft bills of lading attached as a cash item to the credit of the Cotton Company, and at the time of his suicide there had been standing to the credit of the Cotton Company in the bank all of the moneys realized from the sale or con-

version of the cotton, then the situation would have been analogous to the example submitted by plaintiff-in-error. Sears' perfidy, however, did not cease upon securing the cash entries to the credit of the account of the Cotton Company. He thereafter dishonestly dissipated these funds so that at the time of his suicide the Cotton Company was without the cotton or the proceeds realized from its sale to meet the liability incurred upon the acceptances.

For the consideration of the court, we suggest the following illustration:

Assume that on the 19th day of November, 1920, the Cotton Company had on deposit with the Citizens National Bank \$75,000.00 accumulated in previous years' business, and carried in a special account. On this date Sears discovers that he has no money in his checking account to operate the business and that the only assets of the company other than its furniture, fixtures and going concern value is the \$75,000.00 in the special account. On this day a sight draft drawn upon the Cotton Company, attached to which are certain cotton tickets, arrives at the Citizens National Bank and Mr. Sears is informed of its arrival. Mr. Sears then states to the directors of the company: "Let us go and accept this sight draft, take out the cotton tickets, substitute our trust receipt, represent to the bank that upon the sale of the cotton we will return a bill of lading covering the shipment, but when we make a sale of the cotton and secure a bill of lading, we will attach thereto a sight draft drawn upon the purchaser thereof, put the matter through



the bank as a cash transaction; check out the money and use it to run the business.”

Of course, the suggestion, according to the testimony of all the witnesses, would have met with their disapproval. They would not have allowed any such conduct on Sears' part. It is only reasonable to assume that Sears knew that the directors would not allow him to work any such fraud upon the bank, making them and the company liable therefor. Instead of taking the matter up with the directors, Sears, however, reflects with himself as follows: “Well, I will not tell the directors of my scheme. I will keep the matter to myself.” But he does say to the directors, on the 19th day of November, 1920, and frequently thereafter,—“We are making money in the conduct of this business,” and he continues the business, and by the first of May, 1921, he has withdrawn 1091 cotton tickets from the bank, substituting trust receipts therefor, spends the money in conducting the business, but in a manner and for purposes which the directors would not have permitted had they known the facts. On May 19, 1921, the bank being informed of Sears' lack of integrity, withholds (Calif. Civil Code, sec. 3054) \$60,000.00 of the \$75,000.00 (special account), being the value of the cotton tickets wrongfully obtained and converted. In this instance the Cotton Company has lost \$60,000.00 through Sears' duplicity. In other words, if Sears had told the directors of the corporation what he expected to do; if he had told them of the fraudulent plan under which he was going to operate, they would have stopped the fraud in its inception;

but he didn't tell them,—he went ahead and perpetrated his deceits upon all concerned, the bank and the Cotton Company, deceived them both as he proceeded, and during that time when he was perpetrating his fraud and practicing his deceit and duplicity he caused a loss to the Company of \$60,000. The Company has lost that money,—they have become responsible to the bank for that amount, and the bank has taken that amount from their special account. That is the manner in which Sears' duplicity and dishonesty has resulted in a loss and caused the Company a liability, or has imposed upon it a responsibility to the bank. In other words, if Sears had told the truth; if he had conformed his conduct to his representations, such a situation would never have arisen. Because of his duplicity, however, a situation arose which put the Cotton Company in a position where they are required to pay the bank an amount of money, and the source (cotton tickets) relied upon by the Cotton Company to obtain this money, because of Sears' duplicity has vanished.

We conclude this subdivision of our brief by a quotation from the opinion of the learned judge of the trial court [Tr. pp. 179-180]:

“When the cotton market became disturbed and the business as conducted by Sears began to show a loss on purchases and sales, Sears failed in his duty to the bank. After withdrawing cotton tickets or warehouse receipts, and carrying through his sale of the particular cotton, he, in a great many instances, numbering well toward one hundred, failed to replace the withdrawn tickets by outbound documents, which resulted

in the end, in the bank being left with a debt of approximately \$80,000.00 owing to it by the Cotton Company, which was not secured by collateral as the agreement contemplated. The act of Sears was more than a breach of faith; it approached an embezzlement of collateral in which the bank held a qualified property interest. It is argued on behalf of the defendant that the bad conduct of Sears in this regard caused no loss to the Cotton Company, against which only the indemnity had been furnished; that the misuse of the collateral did not cause the Cotton Company to lose what it already owed to the bank. And, furthermore, that whatever criticism might be made of the conduct of Sears, that all of the proceeds which he received were devoted to the business of the Cotton Company and not appropriated by the manager to his own or any other person's use. To my mind, that argument draws too narrow a line in the interpretation of the terms of the bond. The Cotton Company contemplated that its loan account would at all times be protected by collateral received in the usual and ordinary course of its dealings. The securities of the kind first described, when once they reached the bank, if removed under the shifting arrangement referred to, were property for which the Cotton Company was responsible and was bound to return in their resulting equivalent to the bank. The bank was entitled to demand and recover from the Cotton Company the agreed equivalent of the cotton tickets had the equivalent at any time been found in possession of the latter. The unauthorized use of the securities by Sears should be held to amount to a wilful misapplication of property for which the Cotton Company was responsible to the bank. Sears' breach of faith did result in a loss to the Cotton Company, because it would add to its liabilities



the value of the collateral illegally withheld by Sears and used without authority in the business.”

### Point of Plaintiff in Error No. III Answered.

Assignments of error numbers 11 and 26 are by plaintiff in error grouped under the heading:

#### III.

“There is no evidence to support or justify the findings of the trial court as set forth in finding No. VII that the reasonable value of the 1091 bales of cotton sold and disposed of by the Cotton Company, and for which the plaintiff bank held trust receipts was *at the time the same were sold and disposed of*, of the reasonable value of \$60,594.62, or to support finding No. XXIV that the 455 bales of cotton covered by warehouse receipts delivered by plaintiff bank to the Cotton Company prior to December 1, 1920, and not returned to the bank were *at the time they were sold and disposed of*, of the reasonable value of \$29,336.99.” (Br. pp. 49-50.)

### The Facts Involved Under Point III.

We have italicized the phrase “*at the time they were sold and disposed of*” because of the fact that it is a radical departure from the findings. Finding No. VII [Tr. p. 135] is to the effect that the 1091 bales of cotton disposed of by Sears as set forth in the findings “*were at the time of such fraudulent and dishonest conversion*” of the value of \$60,594.62. Finding No. XXIV [Tr. p. 153] is to the effect that the 455 bales of cotton covered by warehouse receipts delivered by plaintiff bank to Sears prior to December 1, 1920, and not returned to the bank “*at the time of their delivery*

by said plaintiff to said J. B. Sears," were of the reasonable value of \$29,337.99 [Tr. p. 153].

The court found:

"That at various times \* \* \* between said 19th day of November 1920, and said 25th day of April, 1921, and in most instances *immediately following* the acceptance of each of said sight drafts \* \* \* with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating, and wilfully misapplying said warehouse receipts, the cotton represented thereby and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained, of thereby causing a loss to said California Cotton & Factorage Company of money, securities and personal property for which it would be, and has, become responsible to the plaintiff herein, said J. B. Sears applied to, and secured from the plaintiff the warehouse receipts then in its possession, \* \* \*." [Finding No. 6, Tr. p. 128.]

"That at said time, and as a part of the same transaction \* \* \* Sears executed and delivered \* \* \* eighty-seven (87) of said trust receipts \* \* \* [Tr. p. 129.] That \* \* \* *pursuant to said fraudulent and dishonest plan and scheme* said J. B. Sears at various times and irregular intervals procured from the plaintiff herein between the 19th day of November, 1920, and said 25th day of April, 1921, fourteen hundred and seventy-six (1476) warehouse receipts \* \* \* and issued and delivered to the plaintiff, in acknowledgment thereof, eighty-seven (87) of said trust receipts." [Tr. p. 130.]

"That subsequent to said 19th day of November, 1920, \* \* \* said J. B. Sears, *pursuant to said*

*fraudulent and dishonest plan and scheme* by him entertained as hereinbefore found, fraudulently and dishonestly converted, misappropriated, and willfully misapplied ten hundred and ninety-one (1091) of said \* \* \* warehouse receipts and ten hundred and ninety-one (1091) bales of cotton represented thereby in the manner following, that is to say:" (Here follows recital of the manner in which Sears having obtained the warehouse receipts sold the cotton covered thereby, surrendered the warehouse receipts and obtained possession of the bills of lading.) [Finding No. 7, p. 131.]

"That said J. B. Sears immediately thereafter, in violation of his duties as secretary \* \* \* and in violation of his promises and representations to the plaintiff, and in violation of the terms of said trust receipts \* \* \* *but pursuant to said fraudulent and dishonest plan and scheme*" (Here follows recital of fraud and deceit practiced by Sears in presenting a draft with bill of lading attached to officers of the bank not acquainted with Sears' transaction with the note department, the securing of approval thereof, the depositing of the same as a cash item, the securing of cash deposit entries upon the bank pass book, the falsification of the books of account of the Cotton Company to disguise and cover up the fraudulent transactions and the subsequent fraudulent and dishonest representations to the officers of the Cotton Company and the bank respecting the making of money by the Cotton Company and the holding of all the Cotton tickets covered by the trust receipts in the possession of the bank, and the belief, reliance and action by the officials of the Cotton Company in the bank upon such fraudulent and dishonest representations.) [Tr. pp. 132-135.]



The evidence discloses [Stipulation, Tr. p. 432]:

“That upon the death of said J. B. Sears said California Cotton & Factorage Company did not have in its possession and did not thereafter surrender to said Citizens National Bank ten hundred ninety-one (1091) of said fourteen hundred and seventy-six (1476) warehouse receipts; that said ten hundred ninety-one (1091) bales of cotton represented thereby cost said California Cotton & Factorage Company *at the time of their purchase* and *were then of the value* of sixty thousand five hundred ninety-four 62/100 dollars (\$60,594.62).”

The evidence also discloses [Stipulation, Tr. pp. 431-432]:

That the four hundred fifty-five (455) bales of cotton covered by warehouse receipts delivered by plaintiff bank to Sears prior to December 1st, 1920, and not returned to the bank *cost* the Cotton Company and *at the time of their purchase were of the value* of twenty-nine thousand three hundred and thirty-seven dollars ninety-nine cents (\$29,337.99).

### **The Law Involved Under Point III.**

The wrongful conversions by Sears date from the time of acceptance of the sight drafts and obtaining possession of the cotton tickets pursuant to the fraudulent and dishonest scheme then entertained and being perpetrated by him; and the value of the cotton tickets at that time, in the absence of any other evidence of value, is conclusive proof of the measure of damages recoverable by the defendant in error.

1. Sedgwick on Damages (9 ed.), Vol. 2, Sec. 497, p. 964.

“Upon general principles, the value of the property at the time of conversion should be the measure of damages, and that is the rule generally adopted.”

2. Sutherland on Damages (4 ed.) Vol. 4.

(a) Section 1112, p. 4222.

“Nothing appearing to the contrary, the date of conversion is presumed to be that at which the property was taken into the possession of the wrongdoer.”

(b) Section 1113, p. 4223.

“In case of the exercise by a lienor of dominion over property where neither the date of the conversion nor the condition of the property at that time is shown, the damage may be proved by showing its value when it came into his possession. If the difficulty of proving value is very great and is the result of the defendant’s act, he will not be relieved from liability on account thereof.”

“If a bailee’s promise is to deliver property valued in his receipt for it at a specified sum he is bound thereby, and if a portion of it is taken from him by process of law he must account for the difference between the value of the whole and of the remainder, regardless of the actual worth of the latter.”

(c) Section 1132, p. 4273.

“The maker of notes which are diverted from their purpose may recover the amount it costs him to discharge them.”

(p. 4277.)

“One who converts a written instrument payable by its terms to himself, but in which another has an interest, must account to the latter for his share of the full sum due according to the face thereof unless he shows its actual value.”

(d) Section 1171, p. 4388.

“Following the principle that the recovery should be commensurate with the injury, if one is fraudulently induced to enter into a contract or pursue a course of action from which expenditures have naturally succeeded or in consequence of which he has been compelled to pay money or devote his time, the expenditures, with interest thereon, \* \* \* will be elements of damage.”

3. 8 Ruling Case Law, p. 489, (Damages Sec. 49).

“Generally the value of property taken or destroyed is to be determined as of the time and place of its taking or destruction.”

4. 8 Cal. Jur. p. 907 (Sec. 140 Damages).

“It has been held repeatedly that evidence of the cost of property of which one has been wrongfully deprived is admissible as a circumstance tending to show its value. While such testimony may have slight probative value only, it may nevertheless be sufficient, in the absence of any counter testimony, to sustain a finding as to value.”

5. California Civil Code, Section 3336.

6. *Anderson v. United States* (C. C. A. 9th Cir.)  
152 Fed. 87, at 91.



7. Angell v. Hopkins, 79 Cal. 181, 183.

“It is quite true that the measure of damages is the value of the property at the time of the conversion with certain additions in certain cases. (Civ. Code, Sec. 3336.) But in arriving at such value, it was proper to take into consideration what the property cost as a circumstance, to aid at arriving at its value at the time in question. (Citing cases)”.

Affirmed in

8. Greenbaum v. Taylor, 102 Cal. 624, 627;
9. Bacigalupi v. Phoenix Building etc. Co., 14 Cal. App. 632, 637;
10. Kirstein v. Berkins V. & S. Co., 27 Cal. App. 586, 589;
11. Union Hollywood W. Co. v. Los Angeles, 184 Cal. 535, 538;
12. Travis Glass Co. v. Ibbetson, 186 Cal. 724, 730.

### **Wilful Trespass Rule Applied in Federal Courts.**

Where the original taking is dishonest or fraudulent, any subsequent act of the wrongdoer which *enhances* the value of the property cannot be permitted to enure to him.

1. Woodenwear Co. v. United States, 106 U. S. 432, 434;
2. Trustees of Dartmouth College v. International Paper Co., 132 Fed. 92, 95;
3. Beechwood Ice Co. v. American Ice Co., 176 Fed. 435, 437;

4. Providence M. & M. Co. v. Nicholson, 178 Fed. 29, 38;
5. Grant v. Fletcher, 283 Fed. 243, 265.

The court having found that Sears obtained the cotton tickets *pursuant to a dishonest scheme to convert and misapply them* and, the plaintiff in error having stipulated that at the time Sears obtained the tickets they had cost the Cotton Company and were then of the reasonable value found by the court, it would seem that the mere statement of these facts refutes the contention of plaintiff in error that there is no evidence to sustain the finding of the court respecting the value of the cotton converted. The argument of counsel for plaintiff in error upon this point is certainly not definite—there are no authorities cited—no principles announced. (Br. pp. 74, 75.) It would appear that their contention on this point is predicated solely upon testimony to the effect that cotton, during the second year, sold on an average of \$12.00 per bale less than cost. This average is for all the cotton sold during the period of the second year [Tr. p. 436] which extended from November, 1920, until May, 1921, (Brief of Pltf. in Error, p. 12) consisting of the 1091 bales fraudulently obtained by Sears from the plaintiff bank as well as all other cotton coming into the hands of the Cotton Company from other sources, including cotton purchased through other banks and cotton purchased directly [Tr. p. 290] and for sales of this cotton occurring as late as April 25th, 1921.

This is no proof at all of what the 455 bales obtained by Sears from the plaintiff Bank prior to December 1st, 1920, were sold for.

Having in mind the rule of wilful trespass hereinbefore referred to and its application where the fraudulent conversion is followed by an *increase* in the value of the converted property, it would appear as a corollary thereto that any diminution in the value of the converted property should be borne by the wrongdoer. Indeed it would be a sad commentary upon the law under any system of enlightened jurisprudence to have it said that one may be dishonestly dispossessed of his property and his measure of damages for the conversion is determined not by the value of the property at the time of such conversion, but by such lesser value as the wrongdoer may later place upon it in consummating a sale thereof. The transactions of Sears subsequent to November 19, 1920, were by the court declared to be fraudulent and dishonest and conducted pursuant to a fraudulent and dishonest scheme.

However, the outstanding fallacy in the argument of plaintiff in error is the contention that the measure of recovery is the value of the cotton tickets *at the time the cotton was sold by Sears*. This is not the correct criterion to determine the liability of the Bonding Company. The liability of the Bonding Company is determined by the extent of the financial responsibility, for which by reason of the perfidy of Sears, the Cotton Company became liable to the Bank as of date of December 1, 1920. In other words, the Bonding Company agreed to reimburse the Cotton Company for



any loss—including the responsibility it incurred to others—by reason of the faithlessness of Sears. The extent of this liability is fixed by the value, *at the time of their conversion* of the 455 cotton tickets converted by Sears prior to December 1, 1920, which it was stipulated [Tr. pp. 431-432] cost the Cotton Company and which were then of the value found and determined by the court, viz: \$29,377.99.

#### Point of Plaintiff in Error No. IV Answered.

Assignments of error numbers 2, 25, 27, 28, and 30 are by plaintiff in error grouped under the heading:

#### “IV.

The Cotton Company during the latter part of 1920 became a corporation sole—to-wit, J. B. Sears, and thereafter J. B. Sears, the ‘risk’ named in the bond, was in complete ownership and control of the Cotton Company. That on and after the date when such complete ownership and control was obtained by J. B. Sears the Cotton Company—to-wit, J. B. Sears, had no right of action to recover for any loss sustained by the wrongful acts of J. B. Sears, whether committed prior to or subsequent to the date on which the ownership and control of the Cotton Company was acquired by Sears. For that reason the trial court erred in finding judgment against defendant and in refusing to grant defendant’s motion for judgment for defendant. In view of the finding of fact that the Cotton Company became a corporation sole—to-wit, J. B. Sears, on December 1st, 1920, the trial court erred in its conclusions of law that the plaintiff (assignee for collection of the Cotton Company) was entitled to judgment for any loss resulting from the wrongful acts of J. B. Sears.” (Brief p. 76.)

### The Facts Involved Under Point IV.

We contend that this point IV is for the first time raised under the writ of error. It was never submitted for the consideration of the trial court. As we read the assignments of error numbers 2, 25, 27, 28, and 30, specified as supporting the point, we conclude that no one or more of them raises the point now presented for the consideration of the appellate tribunal.

Let us examine the specifications of error noticed as supporting Point IV.

1. The first is assignment of error number 2. It specifies as error the overruling of the defendant's motion for nonsuit. In the first place, the record discloses [Tr. p. 377] that no exception was taken to the ruling of the court denying the motion. In the second place all of the evidence bearing on the stock transfer from West to Sears was introduced subsequent to the motion and as part of the defense of the plaintiff in error [Tr. pp. 379-402].

2. The second and fifth are assignments of error numbers 27 and 30. They specify the absence of evidence to support the finding that the stock transfer from West to Sears occurred December 1, 1920, and the failure to find that such transfer occurred prior to November 17, 1920. A consideration of the assignments involves an analysis of the evidence, and does not involve any question of law. These assignments are specifically attacked in Point V of plaintiff in error and the discussion of the assignments under that point as found in the brief of the plaintiff in error

(Br. pp. 95-101) is clearly distinct from and in no manner approaches the question set forth under Point IV now under discussion.

3. The third and fourth are assignments of error numbers 27 and 28. They specify as error the conclusion of the court that the plaintiff is entitled to judgment and the awarding of judgment in favor of plaintiff and against defendant on the ground that the same is contrary to the law, the cause made, the facts pleaded and the records in the action. These same assignments, viz: Nos. 27 and 28 are urged by plaintiff in error as supporting its points numbered I and VI, as well as No. IV (Brief pp. 49, 51). Points Nos. I and VI are fundamentally different one from the other and in their consideration by counsel for plaintiff in error involve essentially different matters of fact and law. (Brief pp. 53 to 66 and pp. 101 to 126.) As they differ one from the other, each of these points also differs from Point IV, and are so considered and presented in the brief of plaintiff in error.

Assignment of error No. 28 is an omnibus assignment clearly in violation of the rules of this court and the principles and practices of all courts requiring definiteness and particularity in the assignment of errors relied upon and intended to be urged.

In the fourth special defense pleaded by the plaintiff in error [Tr. pp. 79-81] it is alleged that West transferred his stock to Sears about May 24, 1920. This was long prior to the first conversions and misappropriations of Sears, which began November 19, 1920. [Pleading Tr. p. 40; findings Tr. p. 126.] The plain-



tiff in error contended before the trial court that the sale from Sears to West occurred about May 24th, 1920. This same contention is again made in this court. (Point V Brief pp. 95-100.) The defendant in error contended before the trial court that Sears never purchased the stock of West and that the title to the stock never passed to Sears. The court accepted the contention of neither party, but found that West sold the stock to Sears and that the title passed December 1, 1920 [Tr. p. 149]. There was never presented to the trial court the question which is now presented upon review, and we entertain very serious doubt whether the point as urged is proper under any of the assignments of error.

#### **The Law Involved Under Point IV.**

Plaintiff in error in its brief (pp. 81 to 95) has cited several authorities, quoting at length from some of them, upon a principle of law that has no application to the matter now before the court. Among these authorities are:

Meily Co. v. London etc. Fire Ins. Co., 148 Fed. 683 (Br. p. 95);

*In re Rieger*. 157 Fed. 609 (Br. pp. 93, 94);

Farmers & Merchants State Bank v. U. S. F. & G. Co. (S. D.), 36 L. N. S. 1152 (Br. pp. 89 to 92);

Frost on Guaranty Insurance (Br. pp. 85, 86, 87, 88, 89).

These decisions are authority for the proposition.

“That the risk shall continue to occupy the position in the employ of the insured designated in the proposal or application for the policy.”

Frost, p. 346 (Br. p. 88).

Stating the same principle in the language of the opinion of the court in the South Dakota case cited:

“The object of the undertaking was to insure an employer against the fraudulent acts of an employe, not to insure an employer against his own fraudulent acts. When the person whose conduct is insured ceases to be an employe within any fair and reasonable interpretation of the term used in the policy, the insurer’s liability should cease, unless he has notice of the change.”

F. & M. State Bank v. U. S. F. & G. Co., 36  
L. N. S. 1152 (Br. p. 91).

Counsel for plaintiff in error states the principle in this fashion:

“A careful reading, however, of this later South Dakota decision does not in any way repudiate the rule announced in the earlier case that a substantial change of relationship between the employer and employe relieves the surety company from liability \* \* \*.” (Br. p. 92.)

The finding of the court [Tr. p. 149] is to the effect that on December 1, 1920, when West sold 496 of the outstanding 500 shares of stock to Sears that Sears thereafter became the practical owner, and for all practical purposes could be considered as the corporation, and as the direct consequence thereof the liability

on the part of the insurer under the bond ceased at that time and the amount of recovery was limited to the extent of the liability which had been incurred prior to December 1, 1920, or prior to the time that Sears ceased to be an employe and became the employer. To restate this simple matter, illustrating the lack of application of the principle announced in the preceding cases, we respectfully submit that the trial court applied the principle by refusing to allow any recovery for liability incurred subsequent to December 1, 1920, and limiting the recovery under the bond to the liability incurred while Sears acted in the capacity of general manager with the ownership of but one share of stock. Counsel for plaintiff in error make precisely this statement, at page 19 of the brief. It is as follows:

“The judgment rendered by the trial court \* \* \* represents the amount paid by the plaintiff bank for the cotton \* \* \* surrendered \* \* \* prior to December 1, 1920 \* \* \*.”

Another principle which plaintiff in error advances is stated as follows:

“An unquestioned limitation on the insurer’s liability is that the claim shall be a valid and enforceable one against the risk in favor of the insured.” (Br. p. 82.)

Several authorities are cited in support of this proposition. We do not dispute that the principle is a correct one, but do dispute the unsupported statement of plaintiff in error that on December 1, 1920, the California Cotton & Factorage Company did not have an



enforcible claim against Sears. If the dishonesty and deception being practiced by Sears were discovered on that date there would have been not only a civil liability on Sears' part for his breach of faith but, as the trial court intimated [Tr. p. 179], a charge of embezzlement might with some justification have been made.

A third principle of law contended for by plaintiff in error and in support of which several authorities are cited may be stated as follows: If necessary to work out equitable ends or to prevent the perpetration of a fraud courts both at law and in equity will look beyond corporate entity to ascertain the real parties in interest. (Br. pp. 84, 85.) This principle is well and briefly stated by the Supreme Court of California in the recent case of *Erkenbrecher v. Grant*, 187 Cal. 7, at 9, 10, as follows:

“While it is the general rule that a corporation is an entity separate and distinct from its stockholders, it is also equally well-settled that both law and equity will, when necessary to circumvent fraud, protect the rights of third persons, and accomplish justice, disregard this distinct existence and treat them as identical.”

This principle was applied by the trial court in limiting the recovery under the bond to such liability as had been incurred prior to December 1, 1920, being the time when, as plaintiff in error contends, the employee became the employer, or the risk became the principal.

The real contention of counsel for plaintiff in error upon this point as we understand it (Brief, pp. 77-79) may be summed up in the following manner:

On December 1, 1920, the Bonding Company was liable to the Cotton Company in the amount specified in the judgment. On this date, however, Sears purchased the stock held by West, and thereafter, for all practical purposes, became the corporation and entitled to all its assets, one of which was the claim under the bond. If allowed to enforce this claim he would be benefiting by his own fraud. Consequently, the claim may not be enforced.

The first error of this reasoning is the assumption that the claim under the bond was assigned to Sears, another is that Sears got control of the stock of West. The fact is, that although the stock was issued in Sears' name and the court found West sold it to Sears, the stock was endorsed in blank by Sears and returned to West, who held it as collateral to secure the purchase price of the stock, no part of which was ever paid. [Tr. p. 388.] A third error in the argument is the assumption that if the judgment is paid by the Bonding Company it will benefit the wrongdoer, Sears, or his estate. The payment of the judgment reduces the liability of the Cotton Company to the Bank, and accordingly reduces the liability of the president of the corporation, T. W. McDevitt, upon the guaranties, and reduces the financial responsibility principally of West upon his stockholder's liability. There can be no doubt of the liability of West as a stockholder of the Cotton Company as of date December 1, 1920.

If Sears were alive today he would not benefit by the judgment, and being dead his estate is in no different position. The persons principally benefiting by the judgment are West and McDevitt. West is relieved of his stockholder's liability, and McDevitt as guarantor upon the acceptances. West, on December 1, 1920, and at all times prior thereto and subsequent to the organization of the Cotton Company owned 496 of the 500 shares of stock issued and outstanding [Tr. p. 149].

At the time of the sale one share was left in the name of West who continued to act as treasurer and director of the corporation. [Tr. p. 382.] The note [Plaintiff's Exhibit No. 18, Tr. p. 383] given in payment for the transfer of the stock discloses that the 496 shares were pledged as collateral. [Tr. p. 384.] The payment of each of the sight drafts is guaranteed by T. W. McDevitt, president of the Cotton Company. [Tr. p. 220.]

An entirely distinct and perhaps more persuasive answer to this point of plaintiff in error is as follows:

If after December 1, 1920, the Cotton Company was a corporation sole, to-wit: J. B. Sears, then for the same reason prior to December 1, 1920, the Cotton Company was a corporation sole, to-wit: T. J. West.

If the courts will look beyond the corporate entity after December 1, 1920, to prevent a fraud they will do likewise prior to December 1, 1920, to accomplish the same purpose. On December 1, 1920, West, as the corporation sole, had a right of action under the bond



against the plaintiff in error because of the liability then existing and of which he had no knowledge. This is the right of action which was assigned to the defendant in error after the discovery of Sears' lack of fidelity. It was never assigned to Sears and his purchase of the stock (incomplete as it was) did not, and was not intended to, transfer such cause of action to him. The willingness of the courts to look beyond the corporate existence is a shield against, and not a weapon for, the commission of fraud and injustice.

The contention of plaintiff in error though specious is ingenious.

Because of a failure to present this question for consideration to the trial court we repeat the following quotation:

“While it is the duty of this court to review the action of subordinate courts, justice to those courts requires that their alleged errors should be called directly to their attention, and that their action should not be reversed upon questions which the astuteness of counsel in this court has evolved from the record.”

Robinson & Co. v. Belt, 187 U. S. 41, 50.

### **Point of Plaintiff in Error No. V Answered.**

Assignments of error numbers 25 and 30 are by plaintiff in error grouped under the heading

#### **V.**

“The court erred in its finding of fact that the control of the Cotton Company did not pass from West to Sears until December 1, 1920.”

## The Facts Involved Under Point V.

The point presented by counsel for plaintiff in error, as well as the two assignments upon which it is predicated, present for this court's consideration no question of law but merely a consideration of conflicting testimony. Indeed, in the discussion of this point in its brief at pages 95 to 100 the plaintiff in error merely presents for the court's consideration excerpts of conflicting testimony of the witnesses. Naturally, the testimony of witnesses supporting the contention of the plaintiff in error is emphasized and set forth at length, while the conflicting testimony of witnesses produced by the defendant in error are referred to in substance and effect and passed over hurriedly. This date, namely, December 1, 1920, is exceedingly important, in that it fixes the time to which the liability of the plaintiff in error extends. Because of the fact that the testimony is conflicting respecting the date, and of the rule of law that this court will not disturb the finding of the trial court if there is substantial evidence to sustain it we shall quote only the evidence which supports the finding. It is as follows:

*Testimony of C. H. Hartke* [Tr. pp. 459-462.]

"I recall the occasion of certain certificates of stock  
\* \* \* being issued in the name of J. B. Sears  
\* \* \*. I had a conversation with Mr. West in connection with that matter \* \* \* Sears was present. This conversation took place about the first day of December, 1920. Mr. West and Mr. Sears  
\* \* \* asked me what the records showed as to the latest date that the stock appeared in the name of Mr.

West \* \* \* and I told them \* \* \* May 20 \* \* \*. That was practically all of that conversation. *Subsequent to that conversation* I know that certificates for 496 shares of stock were issued in the name of J. B. Sears. I can't say exactly as to when those certificates were issued, but it was sometime *after December 1, 1920* \* \* \*. I put my signature as secretary on those certificates along about December 1, 1920 \* \* \*."

(Referring to the erasures appearing upon the original certificates, the witness testified:)

"Mr. Norsworthy made the erasure, not in my presence, but he acknowledged that he had done it along sometime *after December 1, 1920*. He first had written December 1, or the numerals corresponding to that date in there. I did not see him write the date in there but I saw the figures in there before he had made the correction and I recognized them as his handwriting." [Plaintiff's Exhibit 18, Tr. pp. 383-385.]

This note bearing date December 1, 1920, is the consideration for the 496 shares of stock. In view of the fact that the maker of the note is one T. W. McDevitt and that it was endorsed by Sears to West in consideration for the alleged transfer of stock, the date of the note, namely, December 1, 1920, establishes conclusively that the transfer of the stock could not have taken place prior to that date.

### **The Law Involved Under Point V.**

This court will examine the record when a question of law is presented relating to the evidence, not for



the purpose of weighing conflicting testimony, but only to determine whether there was some evidence, competent and substantial, fairly tending to sustain the finding.

Lancaster v. Collins, 115 U. S. 222, 225;

Chicago & N. W. Ry. Co. v. Ohle, 117 U. S. 123, 129;

Troxell v. D. L. & W. R. R. Co., 227 U. S. 434, 442;

Abrams v. United States, 250 U. S. 616, 619.

When an action at law is tried without a jury by a Federal court and it makes a general or special finding of facts, the Act of Congress forbids reversal by the Appellate Court of that finding or of the judgment based thereon "for any error of fact" (Rev. St. Sec. 1011, U. S. Comp. St. 1913, Sec. 1642, p. 700) and a finding of fact contrary to the weight of the evidence is an error of fact.

Wear v. Imperial Window Glass Co., 224 Fed. 60, 63.

When in an action at law a jury is waived and the court tries an issue of fact and makes a special finding upon which the substantial evidence is conflicting, the losing party may not reverse it by writ of error because it was not sustained by the weight of evidence.

Barnsdall v. Waltemeyer, 142 Fed. 415, 417.

A cursory examination of the contention of counsel for plaintiff in error (Brief pp. 95-100) discloses that there was a sharp conflict of testimony respecting the date when the sale from Sears to West became ef-

fective. The trial court accepted the testimony of the witness Hartke which was competent and substantial.

**Point of Plaintiff in Error No. VI Answered.**

Assignments of error numbers 2, 20, 23, 27, 28 and 31 are by plaintiff in error grouped under the heading:

VI.

“There was a breach by the Cotton Company of the promissory warranties made to the Bonding Company and given as consideration for the execution of the bond, and of the provisions of the bond in that the Cotton Company’s books, accounts, stock and securities were not inspected and audited by T. J. West as warranted.”

**The Facts Involved Under Point VI.**

The representation of the Cotton Company respecting the examination of its books by T. J. West is found in the application for bond, Plaintiff’s Exhibit 2, question and answer No. 12 thereof, transcript page 202, reading as follows:

12. (a) At what intervals will applicant’s books, accounts, stocks and securities be inspected and audited and verified with funds on hand or in bank?  
(a) At least once in every.....month. Books checked up each month.

(b) At what intervals and in what manner will outstanding accounts as shown in applicant’s books or reports be verified? (b) We have no such accounts.

(d) By whom will above inspections and audits be made? (d) T. J. West, treasurer \* \* \* official capacity.

In the answer to question 12 (a) in the printed form of application used there appeared printed the following:

“(a) At least once in every.....month.”

The applicant did not fill in the blank but typed in the answer, reading:

“Books checked up each month.” [Tr. p. 144.]

The finding of the court directly in point is finding No. 16 [Tr. pp. 143-146.] This finding is abundantly supported by the evidence appearing in the printed transcript, portions only of which are referred to by counsel for plaintiff in error in its brief, pages 12-16.

For the court's convenience in this matter we set forth the specification of error No. XX in the language of the assignment (Brief pp. 43,44) inserting, however, throughout the specification references to the pages of the printed record where the testimony will be found in support of the finding. It is as follows:

XX.

“There is no evidence to support or justify that part of the finding of fact of the court No. XVI that T. J. West, treasurer of said California Cotton & Factorage Company, ‘visited the office of the said California Cotton & Factorage Company semi-monthly [Tr. p. 330] during the term of said bond as herein found and at such times conferred with J. B. Sears respecting the business of said Company [Tr. p. 330] and checked over the books of said Company [Tr. pp. 330, 334, 338] but not in detail at any time examining the cotton account being the purchase and sales cotton ac-



count [Tr. pp. 330, 334, 338] showing the cotton bought and sold and at said times examined the records disclosing the amount of cotton bought, the amount of cotton sold, the number of bales unsold, the entries respecting the hedging of the same, [Tr. pp. 330, 334, 338] and also examined the cash account and the acceptance account [Tr. pp. 337, 338], together with the cotton tickets indicating the number of bales of cotton on hand and compared the same and determined that they corresponded to the acceptances in the plaintiff bank [Tr. pp. 334, 337, 338], and that at such times said T. J. West checked the books of said Company for the purpose of determining the amount of money owing by said Company to said Citizens National Bank [Tr. pp. 338, 339] and examined the statements and books of said Company and did observe the amount of said cotton purchased [Tr. pp. 337, 338], the number of cotton tickets and bales of cotton on hand, [Tr. pp. 337, 338] and examined the ledger books of said Company and the various accounts therein, including the cotton account, and checked the same with the bookkeeper's statement furnished at the end of each month' [Tr. pp. 334, 337]; or that

'that said T. J. West checked the accounts of said Company, including the bank account, semi-monthly by said statements rendered by the bookkeeper as herein found' [Tr. pp. 334, 337, 338]."

The finding and evidence appearing in the printed transcript at the pages referred to disclose that twice a month West checked up the books of account of Sears and satisfied himself that they were being properly kept and that the Company was making money. He checked the cotton bought, the cotton sold, the cot-

ton tickets on hand, the acceptance account and the cash account.

### The Law Involved Under Point VI.

Counsel for plaintiff in error apparently contends (Br. pp. 101, 111) that the Cotton Company in its application for bond represented that T. J. West, treasurer would at intervals of one month, inspect and audit and verify the applicant's books, accounts, stock and securities with the funds on hand and in the bank. No such representation was made and, as a matter of fact, no such representation is pleaded. We invite the court's attention to the allegation of the special defense [Tr. p. 76]:

"Defendant further avers that pursuant to said application, Exhibit A aforesaid, paragraph 12, subdivisions a and d, the books and accounts of said California Cotton and Factorage Company were to be '*checked up at least once in each month*' by 'T. J. West, treasurer.'"

Then follow the allegations upon information and belief that no audit was made of the books, accounts, stocks and securities of the company nor any inspection, audit or verification of the funds.

As we interpret the application, the California Cotton & Factorage Company did not agree to inspect nor to audit nor to verify the books or accounts or stock or securities with the funds either on hand or in the bank at any stated period, or at all. What it represented would be done was as the Bonding Company pleads, viz: "that the books would be checked up each

month by T. J. West". The plaintiff in error contends that the California Cotton & Factorage Company should, each month, have made such an examination of the books and accounts as would have disclosed Sears' frauds.

A representation that the books and accounts kept by the employee would be examined from time to time in the regular course of business does not mean such a thorough and exhaustive examination as would necessarily discover an irregularity that might exist, however cunningly covered up.

1. U. S. F. & G. Co. v. First Nat. Bank, 233 Ill. 475; 84 N. E. 670, at 673;
2. Title Guarantee & Surety Company v. Nichols, 12 Ariz. 405; 100 Pac. 825 at 830 and 831;
3. Title Guarantee & Surety Company v. Nichols, 224 U. S. 346.

In the case of U. S. F. & G. Co. v. First National Bank, *supra*, the bonding company required the bank to file, prior to the expiration of the bond, a certificate stating that the books and accounts of the employee had been examined from time to time in the regular course of business and had been found correct, and that all moneys handled by him had been accounted for. The filing of such certificate was a condition precedent to the issuance of the renewal bond and the renewal bond was issued on the faith of such certificate of the bank signed by its president. Unknown to the officers of the bank, the employee mentioned in the bond had been guilty of embezzlement at the time



the certificate of the bank president was filed and the renewal certificate issued. Concerning the obligation to examine the books of account, this language is found in the opinion of the court (84 N. E. 673) :

“Appellant insists that the failure of the bank to discover this discrepancy is conclusive proof that no examination was, in fact, made. This conclusion is not warranted by the facts and circumstances in this record. If it be assumed that an examination of the bank’s books means only such a thorough and exhaustive examination as would necessarily discover the slightest irregularity that might exist, however cunningly covered up, then, of course, appellant’s contention would be sound; but this is manifestly not the meaning of the word ‘examination’ in the certificates in controversy. *If bank officers are to be held to such a rigid method of examination and supervision over the accounts of their employees there would be but little necessity, if any, for purchasing fidelity insurance.* When a trusted employee conceives a scheme of criminal misappropriation of his employer’s money, he, at the same time, insures his plans for covering up his wrongdoings. He has many advantages over his employer, since he knows what the real facts are and is therefore always on his guard to allay suspicion, while the employer is ignorant of the real facts and therefore unsuspecting.”

In the case of the Title Guarantee and Surety Co. v. Nichols, *supra*, decided by the Supreme Court of Arizona and afterward affirmed on writ of error from the Supreme Court of the United States, the court

uses the following language in disposing of contentions somewhat analogous to the contentions here made:

“The principal defense was that the loss was due to the neglect of the employer to supervise the conduct of the employee by making such monthly examinations of his account as it agreed to make or have made.” (224 U. S. 349.)

“The obligation in respect to examinations of the employee’s accounts is found in the application. The questions propounded by the Surety Company and the employer’s answers, so far as relevant, were these:

“ ‘To whom and how frequently will he account for his handlings of funds and securities? Monthly; to Board of Directors.

“ ‘What means will you use to ascertain whether his accounts are correct? Examination of books and count of money and securities. How frequently will they be examined? Monthly or oftener. By whom will they be examined? Our auditor.’ ” (224 U. S. 350.)

“The cashier’s embezzlements of money were covered by false entries relating to remittance to the bank’s correspondents, whereby the balances in such banks were made to appear much larger than they actually were. The defendant’s expert evidence tended to show that if the returned vouchers or the reconciliation reports of such banks had been compared with the ledger accounts, the discrepancy would have appeared. But the cashier was cunning, and he testified to the difficulties which he threw in the way of any effort to verify the books in these particulars.” (224 U. S. 352.)

“The mere fact that the examination, if made by a reasonably competent person, failed to discover discrepancies covered up by false entries, or other bookkeeping devices, would not defeat the renewal. The case upon this point went to the jury upon the fact of reasonable examinations and the good faith of the bank in making the representation.” (224 U. S. 353.)

The evidence in this case discloses that West checked the books and accounts of the Cotton Company every two weeks [Tr. p. 330], twice as frequently as was represented in the application, and that West, although a man of many years experience in the cotton business [Tr. p. 330], was deceived by Sears, because of the falsification of the accounts as found by the court [Tr. pp. 133, 134], and the misrepresentation of Sears that the Company was making money and that the cotton tickets in its possession represented profit [Tr. pp. 330, 331].

Counsel for plaintiff in error has cited several authorities (Br. pp. 112-125-126) in support of his contention that

“The failure of the Cotton Company to have T. J. West make a monthly examination, audit and check of the books as agreed, releases the Bonding Company from all liability.” (Br. 111.)

If West had neglected to make a monthly check of the books the decisions referred to and the quotations therefrom and the comments of counsel would be pertinent to the matter in hand. The error of counsel's contention consists in his having taken for granted that which he set out originally to establish (Point 6,



Br. p. 101), namely, that West did not check the accounts as warranted. The court found, upon abundant evidence, that West checked the books and accounts of the Cotton Company semi-monthly. In the decisions cited by plaintiff in error the court in each instance found as a matter of fact that the warranty in regard to inspections had been violated, for example:

(1) *Maryland Casualty Co. v. Bank of England*, 2 Fed. (2d) 793, (Br. p. 112) applicant represented that the cash and securities would be examined and compared with the books, accounts and vouchers monthly. The court found that there had been no monthly comparisons.

(2) In *U. S. F. & G. Co. v. Downey* (Colo.), 88 Pac. 451, 10 L. R. A. (N. S.) 323, (Br. p. 114.) There was represented that the books and accounts would be examined and verified with funds and property on hands and in bank every three months, the facts of the case disclosed that there was no attempt to verify the accounts and that the trustees accepted the figures submitted to them by the employee whose fidelity was assured by the Bonding Company.

(3) In *Young v. Pac. Surety Co.*, 137 Cal. 596. It was represented books and accounts, monies, securities and vouchers would be examined and verified daily. The applicant failed for a period of four days to make such examination and verification, during which time the cashier absconded.

(4) In *Hunt v. Fidelity Casualty Co.*, 99 Fed. 242. The applicant represented that the cash would be com-

pared and verified once a month. A direct verdict for the defendant was based upon the specific ground "that there had been no monthly examination by the assured of the cash and accounts of its agent in compliance with the promise of the assured." (99 Fed. 244.)

(5) In *Ellzey v. Mass. Bonding & Ins. Co.*, 142 La. Ann., column 818, the plaintiff admitted failing to carry out the promise with reference to monthly examination by an auditor or expert accountant.

The other authorities cited by plaintiff in error are to the same effect.

In 10 L. R. A. (N. S.) 323, referred to by counsel for plaintiff in error (Br. p. 114) will be found the following opening statement of the case note published in connection with the Colorado case referred to by plaintiff in error:

"No hard-and-fast rule can be laid down as to what constitutes a verification of accounts in accordance with the requirements of a fidelity contract, especially in view of the paucity of authority on the question. It would seem, however, that, while it is incumbent upon the obligee, in examining the principals' account, to use all means that are palpably within his reach, as was decided by the foregoing case, an examination such as is due and customary with the obligee in his business, if made in good faith, will be a sufficient compliance with such condition in the contract. This was the conclusion reached in *Guarantee Co. of N. A. v. Mechanics' Sav. Bank & T. Co.*, 26 C. C. A. 146, 47 U. S. App. 91, 80 Fed. 766, Affirming 68 Fed.

459, in which it appeared that the bond in question provided that the acts of the principal therein, a bank teller, should be verified by the finance committee of the bank.”

We respectfully submit that the finding of the court, sustained by the evidence as heretofore indicated, shows a *bona fide* and substantial compliance with the terms of the applicant to check the books of Sears monthly.

Heretofore in answer to “Point Number V of Plaintiff in Error” we have cited authorities sustaining the principle that the court will not under the writ of error weigh conflicting testimony, but will confine itself to a determination of whether there was some competent and substantial evidence to sustain the finding. We again refer to these authorities in connection with the finding of the court respecting the monthly examination of the Cotton Company’s books by West.

#### **Point of Plaintiff in Error No. VII Answered.**

The assignments of error numbers 4 to 18, inclusive, and 21 and 24 are by plaintiff in error grouped under the heading:

#### **VII.**

“The Cotton Company had knowledge of the performance by Sears of the acts done by him as secretary and which it is now claimed were dishonest for the reason that the acts done by Sears as expressly plead by plaintiff, were within the scope of his duties as secretary, and were for the exclusive benefit of the Cotton Company in the prosecution of the business for



which it was incorporated. It is not claimed that Sears sought to gain any personal advantage or benefit to himself or to any other person than the Cotton Company.

“The failure of the Cotton Company, having knowledge of the acts of Sears now complained of, to notify the Bonding Company thereof within the time provided in the bond, prevents any right of recovery thereon and estops the Cotton Company from maintaining any action predicated upon the alleged fraudulent acts. In view of this knowledge on the part of the Cotton Company it was an error for the trial court to find that any fraud or deceit was practiced by Sears upon the Cotton Company.”

### The Facts Involved Under Point VII.

The bond contains the following provision respecting notice [Tr. p. 122]:

“This is executed upon the following express conditions, which are conditions precedent to the right of the employer to recover hereon:

2. “\* \* \* That if the employer become aware of the employee committing any act of fraud or dishonesty \* \* \* the employer shall, within ten days thereafter notify the company \* \* \* and the company shall not be liable for any loss subsequently incurred by the employer through any act of the employee unless the company shall have consented in writing to continue its liability under this bond.”

The court found [Tr. pp. 134, 135] that Sears represented to the officers and directors of the Cotton Company that the cash items (deposits) in the bank passbook and the corresponding credits entered upon

the books of account of the Cotton Company represented moneys made and accumulated by Sears in the conduct of the affairs of the Cotton Company and represented to the officers of the plaintiff bank that the Cotton Company still retained, and that he as its secretary had in his custody in the vaults of the Cotton Company, the warehouse receipts surrendered to him, and that the officers of the Cotton Company and the plaintiff bank believed and acted upon such dishonest representations.

The court further found [Tr. pp. 137, 138] that relying entirely upon the deceits practiced upon it by Sears the Cotton Company continued its business subsequent to November 19, 1920, consented to Sears continuing to act as secretary and continuing to administer to its affairs; that it and its officers would not have consented to continuing the business subsequent to November 19, 1920, nor have consented to Sears continuing to act as secretary subsequent to that date or have consented to his conducting any dealings or incurring any indebtedness or contracting any financial obligations in its name or upon its behalf had it or its officers known of the frauds, deceits, dishonesties, wrongful conversions and wilful misapplications, or any of them, practiced upon the Cotton Company and its officers or plaintiff Bank and its officers.

These findings are sustained by an abundance of convincing evidence. Testimony of

(1) T. W. McDevitt (president), Transcript pages 234, 235, 268, 269, 270, 271, 272, 279, 280, 286 288, 291.

(2) John P. Conduit (director), Transcript pages 359-360.

(3) C. H. Hartke (director), Transcript pages 361, 362, 363.

(4) T. J. West (treasurer), Transcript pages 329, 330, 331, 332, 333, 334, 337, 338, 340, 341, 344, 346.

In the brief of plaintiff in error [Tr. pp. 127-131] are many gratuitous statements in direct conflict with the foregoing findings and evidence. The rule of this court (Rule 24) requiring "a reference to the pages of the record" supporting a statement of fact to be discussed, is in all likelihood disregarded by plaintiff in error, not from design, but from necessity.

### The Law Involved Under Point VII.

Although a corporation, like any other principal, is ordinarily chargeable with the knowledge of any facts which are known to its agents upon the principle of imputed notice, this presumption does not arise where the acts of the agent constitute a fraud against the principal, and the disclosure of such facts by the agent would be a disclosure of his own fraud and dishonesty, and in such cases the principal is not bound by such acts of the agent unless it has actual notice.

*American Surety Co. v. Pauly*, 170 U. S. 133;

*Henry v. Allen*, 151 N. Y. 1;

*Benedict v. Arnoux*, 154 N. Y. 715;

*Kettlewell v. Watson*, 21 Ch. Div. 685.

Irrespective of the common law duty of the assured to notify the surety of the frauds of the employee,



and wholly irrespective of the principle of imputed knowledge or any exception thereto, the parties to this bond have by express condition of the same (*contemplating actual notice*) declared the responsibility of the assured in the matter of notice.

Guarantee Company of North America v.  
Mechanics' Savings Bank & Trust Company,  
183 U. S. 402;

First National Bank of Crandon v. U. S. F. &  
G. Co. of Baltimore, 150 Wis., 601, 137 N.  
W. 742-745;

Remington v. Fidelity & Deposit Co. of Mary-  
land, 27 Wash. 429, 67 Pac. 989;

Bank of Willow Lakes v. Syverson, 43 S. Dak.,  
295, 178 N. W. 989.

### **Imputed Knowledge.**

#### *(a) Statement of the Principle.*

The fraudulent acts of Sears were performed within the line of his employment. It is so alleged in the complaint and established by the proof. We have never contended otherwise. It is only the acts performed by Sears "while in the performance of his duties as secretary in the service of such employer and occurring during the continuance of this bond" that are covered by the terms of the bond. Can the Cotton Company upon application of the principle of imputed knowledge be held to have been familiar with Sears' dishonesties? We think not. We predicate our statement upon the propositions, first that the doctrine of imputed knowledge is based upon the rebuttable

presumption that the agent will disclose his information to the principal, and, second, that the presumption is overcome by a showing that such a disclosure would expose the agent's fraud and defeat the objects thereof.

We do not take issue with the principle as stated in the case cited by counsel for defendant, *McKenney v. Ellsworth*, 165 Cal. 326 at 329, to the effect that:

"The familiar rule that the principal is bound by the knowledge of his agent, acquired in the course of the agency *rests upon the presumption* that the agent will communicate to the principal the facts learned by him as it is his duty to do \* \* \*. If the agent is in fact acting for his principal in the transaction, even though he may have an opposing personal interest 'it is his duty, notwithstanding his interest, to communicate to his company (principal), any facts in his possession, material to the transaction, and the law will, therefore, presume *in favor of third persons*, that he made such communication.' "

This decision has been subsequently affirmed by our courts of review. We believe it to be authority for the proposition that the rebuttable presumption supporting the doctrine of imputed knowledge is not overcome by showing that the agent "may have an opposing *personal interest*." This is not quite the case before the court, and does not quite meet our contention unless it can be said that *personal interest* on the part of the agent is the same as *fraud* on the part of the agent.

In the Ellsworth case (165 Cal. 326) a bank president who had actual control of its affairs, and who personally directed the discount by it of a promissory note belonging to himself, had failed to endorse a payment thereon. In an action by the bank upon the note the court declared that the maker was entitled to show the partial payment, the bank being held to have notice of the payment notwithstanding the personal interest of the president therein involved. There were no charges of fraud or deceit involved and such elements did not enter into the considerations of the court.

In support of our contention of the rule, as we have stated it, we rely upon:

1. American Surety Company v. Pauly, 170 U. S. 133.

“Ordinarily a corporation, like any other principal, is chargeable with the knowledge of any facts which are known to its agents; but in this case all these transactions, if there were any transactions of a *fraudulent and dishonest character* on the part of the cashier, were transactions for the benefit of Collins, and he was a *participator in the fraud*, and under those circumstances the law *does not infer* that the agent or the officer will communicate the fact to his principal, the corporation, and under such circumstances the corporation *is not bound* by his knowledge. So this defense melts away and there is nothing of it whatever.” (Page 150.)

Sears was interested in the perpetration of the frauds committed by him in the sense that from the



profits of the corporation, if any, he was entitled to twenty-five per cent thereof, with a five thousand dollar minimum guarantee. [Tr. p. 199.]

Further quoting from the Pauly case:

*"The presumption that the agent informed his principal of that which his duty and the interest of his principal required him to communicate, does not arise where the agent acts or makes declarations not in execution of any duty that he owes to the principal, nor within any authority possessed by him, but to subserve simply his own personal ends or to commit some fraud against the principal. In such cases the principal is not bound by the acts or declarations of the agent unless it be proved that he had at the time actual notice of them, or having received notice of them, failed to disavow what was assumed to be said and done in his behalf."* (Pages 156 and 157.)

Although Sears' acts were within the course of his employment as secretary of the Cotton Company, they were in the particulars alleged in the complaint dishonestly and fraudulently performed, and were performed to carry into effect a dishonest scheme conceived and executed by him which would have failed in its inception had his principals known of his deceits and duplicities.

2. Henry v. Allen, 151 N. Y. 1.

"The general rule that notice to the agent, while acting within the scope of his authority and in regard to a matter over which his authority extends, is notice to the principal, *rests upon the duty* of disclosure by the former to the latter of

all the material facts coming to his knowledge with reference to the subject of his agency and upon the *presumption that he has discharged* that duty. (Citing authorities.) This presumption, however, does not always arise, for there are *several exceptions* well recognized by the authorities. Thus, when the agent has no legal right to disclose a fact to his principal, or he is *engaged* in a *scheme to defraud* his principal, the *presumption does not prevail*, because he cannot in reason be presumed to have disclosed that which it was his duty to keep secret, or that which would *expose and defeat his fraudulent purpose*. (Citing authorities.) As Mr. Pomeroy says in his work on Equity Jurisprudence: ‘When an agent or attorney has in the course of his employment *been guilty of an actual fraud*, contrived and carried out for *his own benefit*, by which he intended to defraud, and did defraud, his own principal or client, as well as perhaps the other party, and the *very perpetration* of such fraud *involved the necessity of his conceding the facts* from his own client, then, under such circumstances, the principal is not charged with constructive notice of facts known by the attorney, and thus fraudulently concealed. In other words, if, in the course of the *same transaction* in which he is employed, the agent commits an independent fraud for his own benefit, and designedly against his principal, *and it is essential to the very existence* or possibility of such fraud that he should conceal the real facts from his principal, *then the ordinary presumption* of a communication from the agent to his principal *fails*; on the contrary, a presumption arises that no communication was made, and conse-

quently the principal is not affected with constructive notice.' (Section 675)." (Pages 9 and 10.)

3. *Benedict v. Arnoux*, 154 N. Y. 715, 728.

"It affirmatively appears in the case that Booth knew nothing of the transaction. It is claimed, however, that the knowledge of his agent is *imputable* to him. This is true to a limited extent; so long as the agent acts within the scope of his employment *in good faith*, for the interest of his principal, he is presumed to have disclosed to his principal all the facts that come to his knowledge as agent; but just as soon as the agent *forms the purpose of dealing with his principal's property for his own benefit and advantage*, or for the benefit and advantage of other persons who are opposed in interest, he ceases, in fact, to be an agent *acting in good faith* for the interest of his principal, and his action thereafter based upon such purpose is deemed to be in fraud of the rights of his principal, and the presumption that he has disclosed all the facts that have come to his knowledge no longer prevails. *The citation of authorities to sustain this proposition is hardly necessary, but it may not be out of place to call attention to the case of Henry v. Allen.*" (Page 728.)

4. *Kettlewell v. Watson*, 21 Chancery Division 685.

"There is another principle which undoubtedly is well established, and is an *exception* from the doctrine of imputed notice, that which is familiarly known by reference to the case of *Kennedy v. Green*. There it was held that the presumption which arises from the duty of the agent to com-



municate what he knows to his principal, *may be repelled* by showing that, whilst he was acting as agent, he was also acting in another character, viz, as a *party to a scheme or design of fraud*, and that the knowledge which he attained was attained by him in the latter character, and that therefore there is no ground on which you can presume that the duty of an agent was performed by the person who filled that double character. That I understand to be the principle of that class of cases." (Page 707.)

This exception to the general principle applies as well to corporate principals as to personal principals. It was a *corporate principal* that was involved in the *Pauly* case, and the case of *Henry v. Allen*.

As we understand, counsel for plaintiff in error contends that whenever the agent possessed of the knowledge is a director of a corporation or general manager of a corporation, then he is the corporation and the corporation as such has the knowledge. We take issue with counsel upon this proposition, and assert that there is no authority to sustain the contention and declare that the authorities we have cited, particularly the *Pauly* case, is to the contrary. In the *Pauly* case, the president, Collins, and the cashier, O'Brien, were the parties perpetrating the fraud. They were the chief executive officers of the bank, and we think it reasonable and fair to argue that it would be difficult ordinarily to experience an instance in the commercial world where the officers of a corporation could be said to be closer or less far removed from the fictitious corporate entity than the president and cashier of a

bank in a community of moderate size. The entire fraudulent conduct of O'Brien and Collins in making the false and dishonest entries of credit to the account of Collins were performed as cashier and president of the Bank. The Bank as a corporation, however, did not know it, did not participate in a fraud upon itself and the Bonding Company was required to indemnify the Bank for its loss (so far as the liability thereunder would do so).

In its final analysis, the doctrine of imputed knowledge merely furnishes a legal theory upon which a principal may be held. The courts do not declare that the principal had actual knowledge of the facts; they declare merely that the principal's liability is the same as though it had actual knowledge.

(b) *Application of the Principle.*

Whether the principle of imputed knowledge and the exception thereto is correctly stated by counsel for the plaintiff in error or by ourselves, or by neither of us, we contend it is of no consequence in the matter now before the court for the reason that the Bonding Company and the Cotton Company entered into a contract defining the duty of Cotton Company concerning any act of fraud or dishonesty of Sears. Let it be assumed for sake of argument that the doctrine of imputed knowledge applies in this case without the limitation of the exception as we have contended. Still the Bonding Company cannot escape liability if they are otherwise responsible for the reason that they have specifically agreed with the Cotton Company

that it is only when the Cotton Company has actual knowledge of the facts constituting fraud or dishonesty that it is required to notify the insurer. Quoting from the bond:

“This bond is executed upon the following express conditions; which are conditions precedent to the right of the Employer to recover hereunder;

2. \* \* \*, that if the Employer *become aware* of the Employee committing any act of fraud or dishonestly, \* \* \* the employer shall \* \* \* notify the company, \* \* \*, and the company shall not be liable for any loss subsequently incurred \* \* \* unless the company shall have consented \* \* \* to continue its liability. \* \* \*.” [Tr. p. 206.]

Irrespective of the common law duty of the assured to notify the surety of the frauds of the employee, and wholly irrespective of the principle of imputed knowledge or any exception thereto, the parties to this bond have by express condition of the same declared the responsibility of the assured thereunder. In support of our contention in this particular, we invite the court's attention to the case of Guarantee Company of North America v. Mechanics' Savings Bank & Trust Company, 183 U. S., 402. This was a suit in equity to enforce an account on bonds of fidelity insurance, one covering the employee as teller and collector, and the other as cashier of the bank.

“In addition to the provisions already mentioned, it was agreed ‘that the employer shall at once notify the company, on his *becoming aware of the said employee being engaged in speculation*



or gambling, or indulging in any disreputable or unlawful habits or pursuits.'” (Page 417.)

“The evidence showed that in the summer or fall of 1892. the cashier of the bank was told that the teller was part owner in a concern engaged in speculative business; he at once informed the president of the bank; and also called Schardt’s (employee covered by the bond) attention to the matter, who admitted that he had once been engaged in such a concern, but said he had sold out, and also that he had speculated to some extent, but had ceased to do so.” (Page 418.)

It also appears that the bank received an anonymous letter that Schardt was speculating. This matter came to the attention of the president of the bank, and through a second director, to a third director and member of the Finance Committee. It also appears that the directors had the matter up with Schardt, who admitted that he had been, but denied that he then was engaged in stock speculation. The court asks:

“In these circumstances was it the duty of the bank to notify the company of what it had heard?” (Page 418.)

The Pauly case is then referred to and the doctrine quoted to the effect that where a bond is fairly susceptible of two constructions, one favorable to the assured, and the other to the surety company, the former should be adopted. The court proceeds:

“But this rule cannot be availed of to refine away terms of a contract expressed with sufficient clearness to convey the plain meaning of the

parties, and embodying requirements compliance with which is made the condition to liability thereon.

“Whatever the common law duty on the part of the employer to notify the guarantor of the fraud or dishonesty of the employee, whose fidelity is guaranteed, the parties to this contract undertook to declare the duty of the bank to the company in *certain specified particulars*. It required that the employee should not have been guilty of previous default or dereliction *within the knowledge* of the employer. It provided for notification of any act of the employee which might involve a loss without unreasonable delay after the occurrence of the act came *to the knowledge* of the employer. And it required immediate notification on the employer *becoming aware of the employee being engaged in speculation or gambling*.” (Page 419.)

It is important to note that the words “*becoming aware*” hereinbefore italicized in the opinion of the Supreme Court are the identical words used in the bond under consideration in the provision hereinbefore quoted. The court then calls attention to the language of the Pauly case requiring “notice of any act on the part of the employee which may involve a loss for which the company is responsible” and to the holding that this clause did not require notice when the suspicion of the bank was aroused. Then this significant statement appears in the opinion.

“But the bond before us not only contained that clause but the clause under consideration, which

was a different and additional clause *intended to secure the safety of prevention* through timely warning.”

“It seems to us that the obvious meaning of ‘*becoming aware*,’ as used in this bond is ‘to be informed of,’ or to be apprised of’ or ‘*to be put on one’s guard in respect to*’ and that no other meaning is equally admissible under the terms of the instrument. These are the definitions of the lexicographers, distinctly deducible from the derivation of the word ‘*aware*’, and that is the sense in which they are here employed. \* \* \*. Our understanding of the provision is that what the company stipulated for was prompt notification of *information by the bank* in regard to speculation or gambling on the part of the employe.” (Page 420.)

Reference is then made to language appearing in the opinion of the Circuit Court, and in the opinion of the Circuit Court of Appeals relating to the question of bad faith or bad judgment on the part of the bank officials. The court then says:

“The company’s defense did not rest on the duty of diligence growing out of the relation of the parties, but *on the breach of one of the stipulations entered into between them*. The question was not merely whether the conduct of the bank *was contrary to the nature of the contract, but whether it was not contrary to its terms.*” (Pages 421-422.)

“The truth is that in spite of strict supervision and the pursuit of the best systems of keeping accounts, there is always a risk of defalcation. The



prevention of defaults or their detection at the earliest possible moment are of even more vital importance to financial institutions than to the guarantors of the fidelity of their employees. The provisions intended to protect the company in this case were not in themselves unreasonable and so far as they operated to compel the bank to exercise due supervision and examination, and due vigilance, were consistent with sound public policy. We think it was the duty of this bank to have made prompt investigation, or at all events to have notified the company at once of the information that it had, and we decline to hold that the bank's misplaced confidence in Schardt affords sufficient ground for enforcing the liability of the surety company on the theory of good faith.

“Our conclusion is that the failure of the bank in the particulars adverted to defeats a recovery on the teller's bond for defalcation *after information of Schardt being engaged in speculation was received.*” (Page 422.)

First National Bank of Crandon v, U. S. Fidelity & Guaranty Company of Baltimore, 150 Wis. 601; 137 N. W. 742, at 745, is authority for the proposition that the notice or information which the employer must immediately indicate to the insurer under penalty of releasing the insurer for failure so to do is *actual knowledge* and does not include constructive notice. Points 3 and 4 found discussed upon page 745 of the 137 N. W. Reporter, contain clear declarations of this principle. For example, it is said:

“The finding of the Circuit Court negatives *actual knowledge* of the practice of kiting checks after the time stated. It is true there is evidence in the case from which the court might have found that such knowledge existed, but the officers of the bank denied having such knowledge, and a finding in accordance with their testimony is fairly supported by the evidence. \* \* \* The language of the bond is that the employer would notify the defendant of certain facts if the same should ‘come to the knowledge of the employer.’ *We interpret this provision of the bond to mean actual knowledge and not mere constructive notice*, which is a very different thing from knowledge, although in some cases its legal effect may be the same. The bond did not require the plaintiff to notify the defendant of matters of which it had knowledge and *also of matters of which it might have had knowledge had its officers made a critical examination of its books from time to time.*” (Page 745.)

There was no possibility of the Cotton Company acquiring actual knowledge of the information possessed by Sears upon the theory of imputed knowledge. In other words a holding to the effect that the knowledge of Sears is imputed to the corporation, which in turn, under penalty of forfeiture of the coverage of the bond, must have conveyed the information to the Surety Company, is to declare that the Cotton Company was required to inform the Bonding Company of matters never coming to the knowledge of the Cotton Company. To state the matter in a different manner, the assured would be deprived of the benefit of the

bond for failure to do that which was humanly impossible, namely, to impart information which it did not itself possess, and in violation of the express provision of the bond applying to actual knowledge.

The case of *Remington v. Fidelity & Deposit Company of Maryland*, 27 Wash. 429; 67 Pac. 989, was an action against an insurer to recover upon a fidelity bond of the cashier of the plaintiff. The bond contained a provision requiring the employer to immediately notify the Insurance Company of any default on the part of the employee. It was contended by the defendant that there had been a breach of this condition. Respecting this defense the court says:

“Bonds of this character are, in their nature, insurance contracts, to indemnify the employer against the dishonesty of employees. They are issued for profit, and the same rules of construction must apply thereto as apply to other insurance contracts. \* \* \* The provisions in the contract above quoted are for the protection of the insurance company. They were not intended to avoid an existing liability under the contract, or as a means of defeating recovery thereon, but only to prevent further liability *after discovery* of dishonesty by the employer. For such purpose the provisions are reasonable and will be maintained, but *if they are to be considered as a shield* to avoid a liability legally and rightfully due, or to avoid a contract properly, made, they are a fraud upon the rights of the insured, and cannot be upheld.” (Page 991.)

It is our contention that the doctrine of imputed knowledge has no application because of the fact that



“the parties to the contract undertook to declare the duty of the (employer) to the (Bonding) Company in certain specified particulars.”

Guarantee Co. v. Mechanics' Bank & Trust Co.,  
183 U. S. 402, at 419.

Further in this connection we quote from a decision of the Supreme Court of South Dakota:

“The application and policy constitute the entire contract between the bank and the company, and the courts are without power to interpolate into it conditions wholly foreign to its express or implied provisions.” (Bank of Willow Lakes v. Syver-son, 43 So. Dak. 295, 178 N. W. 989, at 991.)

## Conclusion.

The motion to strike the bill of exceptions is well taken. There is no attempt made to set out any “very extraordinary circumstances” justifying the trial court in settling and certifying the bill after the expiration of the term. The trial court's action is attempted to be justified upon the doctrine of estoppel. (Br. pp. 30, 31). In the brief of plaintiff in error no mention is made of the leading and recent case of Exporters etc. Inc. v. Butterworth-Judson Co., 258 U. S. 365, and the many more recent decisions pointing it out as the last authoritative word upon this subject. Had counsel for plaintiff in error been familiar with this decision they would not have relied upon the doctrine of estoppel.

Because of the failure to obtain a ruling or request a ruling upon the motion of plaintiff in error for a declaration of law and special findings in its favor

[Tr. p. 466], and because of a failure to save an exception to a ruling or a failure to rule upon such motion only two questions are open to review under the writ.

Of these the first—

The alleged insufficiency of the complaint—is not argued or presented here for review. The sufficiency of the complaint is apparent upon a casual examination, as must be conceded because of the failure of plaintiff in error to contend to the contrary.

In a consideration of the second, viz:

The sufficiency of the findings to sustain the judgment—we are met at the outset with the problem as to whether this question is raised by any proper assignment of error. Unless the question is presented by assignment No. XXVII [Tr. p. 535] it is not presented at all. In this brief we have proceeded upon the theory that the question is properly and adequately raised by this assignment.

That the findings support the judgment we believe will be manifest to the court long before the end of this exceedingly lengthy brief is reached by those who are compelled to examine it.

For the consideration of the court we urge the granting of the motion to strike the bill of exceptions and an affirmance of the judgment.

Respectfully submitted,

WM. J. HUNSAKER,

E. W. BRITT.

T. B. COSGROVE,

*Attorneys for Defendant in Error.*

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IN THE  
United States  
Circuit Court of Appeals,  
FOR THE NINTH CIRCUIT.

---

Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Corporation,

*Defendant in Error.*

---

Notice of Motion to Strike Bill of Exceptions of  
Plaintiff in Error From the Record.

---

WM. J. HUNSAKER,

E. W. BRITT,

T. B. COSGROVE,

*Attorneys for Defendant in Error.*





IN THE  
United States  
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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Corporation,

*Defendant in Error.*

Notice of Motion to Strike Bill of Exceptions of  
Plaintiff in Error From the Record.

*To Plaintiff in Error, Maryland Casualty Company,  
a Corporation, and to W. S. Bicksler, W. C.  
Smith and Dale H. Parke, Its Attorneys:*

You will please take notice that on Wednesday, the 14th day of October, 1925, at the hour of ten-thirty o'clock a. m. of that day, or as soon thereafter as counsel may be heard, the defendant in error, Citizens National Bank of Los Angeles, will move the above entitled court, at its courtroom in the U. S. Post Office building, Seventh and Mission streets, in the city and county of San Francisco, state of California, to strike

from the record the Bill of Exceptions herein of the plaintiff in error.

The motion to strike said Bill of Exceptions from the record will be made upon the following grounds:

I.

That said cause was tried before the Hon. William P. James, one of the judges of the District Court of the United States for the Southern District of California, Southern Division, sitting at Los Angeles, California; that findings of fact and conclusions of law were signed and filed on the 7th day of March, 1925, and judgment entered thereon on the 9th day of March, 1925; that the term of court at which said judgment was entered was the January term; that said term expired on Sunday, July 12th, 1925; and that the Bill of Exceptions herein was not settled or signed until the 29th day of July, 1925.

II.

That the term of court at which the action was tried, the findings signed and the judgment entered had expired; that no order of the court, or of any judge thereof, had been made or entered, neither had the consent of the defendant in error or any of its attorneys been given, extending the time within which to settle said Bill of Exceptions beyond the term in which said action was tried and said judgment entered; that no motion for new trial, or any other motion or proceeding in said action, was pending and undisposed of upon the termination of said term of



court in which said action was tried and said judgment entered; and that no very extraordinary circumstances were shown to justify the court in settling and signing said Bill of Exceptions after the term had expired in which said judgment was entered.

III.

That said court and the judge thereof were without jurisdiction to settle said Bill of Exceptions.

IV.

That the Bill of Exceptions has been settled, signed and certified to this court in contravention of law, in that the term had expired before the same was offered for settlement.

The said motion to strike said Bill of Exceptions from the record will be based upon the records, files and proceedings in said cause, the Bill of Exceptions of plaintiff in error and the printed transcript of record upon writ of error herein.

WM. J. HUNSAKER,

E. W. BRITT,

T. B. COSGROVE,

*Attorneys for Defendant in Error.*



No. 4685.

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IN THE  
United States  
Circuit Court of Appeals,  
FOR THE NINTH CIRCUIT.

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Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

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BRIEF OF PLAINTIFF IN ERROR.

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W. S. BICKSLER,

W. C. SMITH,

DALE H. PARKE,

*Attorneys for Plaintiff in Error.*

FILED

SEP 22 1925

F. D. MONCKTON





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No. 4685.

IN THE

United States

Circuit Court of Appeals,

FOR THE NINTH CIRCUIT.

---

Maryland Casualty Company, a Corporation,

*Plaintiff in Error,*

*vs.*

The Citizens National Bank of Los Angeles, a Banking Corporation,

*Defendant in Error.*

---

BRIEF OF PLAINTIFF IN ERROR.

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History and Nature of the Case.

This action was filed by The Citizens National Bank of Los Angeles (hereinafter referred to as plaintiff bank) as assignee of California Cotton & Factorage Company, a corporation, (hereinafter referred to as cotton company) against the Maryland Casualty Company, a corporation (hereinafter referred to as bonding company) in the Superior Court of the state of California, and thereafter removed to the United States District Court. It was first tried before Judge

Oscar A. Trippet, whose death occurred before decision was rendered; thereafter it was again tried before Judge Wm. P. James, who rendered judgment for plaintiff bank, and the defendant, bonding company, sued out writ of error to this court.

The California Cotton & Factorage Company, plaintiff's assignor, is a California corporation organized in September, 1919, for the purpose of buying and selling cotton on the market. Its authorized capital stock is \$100,000.00, divided into 1000 shares of the par value of \$100.00 each. The subscribed total capital of \$50,000.00 was paid in by T. J. West of Calexico [page 336] and there was issued to him 496 shares of the par value of \$49,600.00 [page 149.] The four remaining shares were issued to J. B. Sears, C. H. Hartke, Thomas W. McDevitt, and J. P. Conduit. They paid no consideration for the shares of stock so issued to them, same being issued solely to qualify them as directors [page 336]. McDevitt was elected president; C. H. Hartke, vice-president; T. J. West, treasurer; and J. B. Sears, secretary; and they, together with the said Conduit, constituted the officers and directors of the corporation during all the period of time in issue, except that Hartke acted as secretary for the period beginning May 20th, 1920, and ending Sept. 9, 1920. J. B. Sears, as secretary, was the general manager of the cotton company, and for all general purposes had complete charge of the cotton company's affairs from the date of its organization.

About December 1st, 1919, J. B. Sears applied to the bonding company for a fidelity bond in the penal

sum of \$50,000.00 in favor of the cotton company, and such bond was issued by the bonding company on December 19, 1919 [bond set forth on page 17]. Sears died on May 3, 1921, and shortly thereafter the cotton company alleges that it ascertained for the first time that by reason of certain acts of Sears while acting as its secretary the company sustained a loss in excess of the penalty of the bond. The cotton company filed proof of loss with the bonding company on July 22nd, 1921. Thereafter on September 1st, 1921, the cotton company assigned its alleged cause of action on the bond to the plaintiff bank. Plaintiff filed suit thereon on May 11, 1922.

## NATURE OF ISSUES.

### (A) Complaint.

Plaintiff bank in its complaint sets forth two causes of action. The first charges in brief that by reason of the misapplication by J. B. Sears, as secretary of the cotton company, not to his own use but to the use of the cotton company, of 1091 warehouse or cotton compress receipts entrusted to the cotton company by plaintiff bank, the warehouse receipts were lost to the plaintiff bank and that the cotton company, being responsible (liable) therefor to the bank, a loss to the extent of such liability was sustained for which loss it is claimed the bonding company is liable.

The second cause of action charges misapplication by Sears to his own use of funds of the cotton company. Judgment was for defendant on this cause of action and the matter therein contained is not at issue on this review.



Defendant demurred to the first cause of action as originally pleaded, which demurrer was sustained [page 39.] Thereupon an amendment was filed and a general and specific demurrer was filed to the cause of action as amended [page 33], which demurrer was overruled, and the overruling of said demurrer is one of the assignments of error presented on review.

**(B) Answer.**

Defendant filed several defenses to the first cause of action. The first defense is a specific denial [page 60].

The second defense pleads that the cotton company breached certain of the promissory warranties, in consideration of which the bond sued upon was issued [page 74], and particularly the warranty that the books and accounts of the cotton company would be checked and audited regularly each month by T. J. West, treasurer. Defendant alleges that the failure of the cotton company to have its books checked and audited as agreed was the cause of any loss sustained.

The third defense [page 78] pleads failure of the cotton company to notify defendant bonding company of the alleged loss within the time expressly provided in the bond.

The fourth defense [page 79] pleads in substance that the cotton company was from the date of its incorporation until May 24, 1920, a corporation sole—to-wit, T. J. West, by reason of the fact that said West was the owner of all the issued stock of the corporation, and that on May 24, 1920 (being a date

prior to the doing by J. B. Sears of any of the acts upon which the alleged loss is based), West sold and transferred to Sears all of said corporate stock, and that thereafter and during all the times when it is alleged the cotton company sustained losses by reason of the acts of Sears the cotton company was in fact a corporation sole—to-wit, J. B. Sears, and by reason thereof all liability on *the bond* insuring Sears' fidelity to the cotton company was extinguished.

The fifth defense pleads in substance that the transactions between plaintiff bank and the cotton company, whereby certain securities, to-wit: cotton tickets were surrendered by the bank to the cotton company, was without fraud or misrepresentation, and that the manner of sale and disposition of the proceeds of the cotton covered by the tickets was known to and approved of by the plaintiff bank, and that the cotton company or plaintiff bank sustained no loss by reason of any fraud or dishonesty or willful misapplication of the bank's property by J. B. Sears.

### Statement of Case.

Immediately after the cotton company was organized it arranged with plaintiff bank for a line of credit to the extent of \$200,000.00, and arranged to have the plaintiff bank loan to it the money with which to purchase cotton, such money to be repaid from the sale of the cotton. This arrangement between the cotton company and the bank was made by Sears, secretary of the cotton company, and confirmed by a letter to plaintiff bank dated September 8, 1919 [page 212],

a portion of which letter succinctly states the way in which the matter should be handled as agreed upon, to-wit:

“The purpose of the Corporation is the buying, selling and the handling of cotton in bale form in all its different branches, or in other words to do a general legitimate cotton business, which will at all times be on a regular basis and as far from speculation as possible.

“The financing of the cotton bought or sold will at all times be protected by collateral either in the form of Warehouse Receipts or Railroad Bills of Lading, which will be held by the Bank as security together with actual daily balances. These Warehouse Receipts or Bills of Lading will at times have to be replaced with Trust Receipts, in order to facilitate the movement of the cotton, for example in making shipments from the different interior points, it is necessary to have the Warehouse Receipts in order to secure the cotton and get Bills of Lading for shipments and at such times Trust Receipts will be issued by ourselves until we can secure the Outbound Bills of Lading, after which time Bills of Lading attached to Sight Drafts are returned to the Bank and the Trust Receipts taken up.

“All purchases or sales will at all times be protected, either by Actual Sales or Purchases or Hedged in the New York or New Orleans Future market.

“The manner of payment for actual cotton bought will be in the form of Acceptances protected by Warehouse Receipts or Bills of Lading covering the actual number of bales of cotton bought or sold, which will also be covered by Insurance in the form of a Blanket Policy for the amount of \$100,000.00.



"It is the purpose of the Company at all times to carry sufficient daily balance to protect its trades, as well as security with collateral attached.

"The total amount of the Acceptance account will vary according to the promptness in making shipments and we do not at any time expect to carry a stock of more than three to five hundred bales and this stock will be covered by actual sales or hedges.

"The Acceptance Account will in some instances run as high as \$150,000.00 to \$200,000.00, but as an average this will probably be between \$50,000.00 to \$75,000.00, which will be protected by either Warehouse Receipts or Bills of Lading."

This letter was received by the plaintiff bank on or about the 8th day of September, 1919 [page 215]. Trust receipts were printed in form as set forth on page 25 of the record herein. Thereupon, the cotton company began the purchase of cotton from the various cotton growing sections, purchases being made through its agents in the field. The cotton so purchased was paid for by drafts drawn upon the cotton company through plaintiff bank with compress or warehouse tickets attached covering the cotton so purchased. When these drafts so drawn on the cotton company arrived at Los Angeles, they were accepted by the cotton company through J. B. Sears, secretary and general manager (a few being accepted by other employees), and the drafts so accepted were then paid by the plaintiff bank for the account of the cotton company, and thereupon the drafts so accepted were held by the plaintiff bank in its collection department as bills receivable due from the cotton company.



Thereafter and from time to time as business required, the cotton company secured delivery to itself from the plaintiff bank of the cotton tickets or warehouse receipts which the bank held as security for the payment of the drafts, and the cotton company substituted in lieu of said cotton tickets so delivered to it, a trust receipt. The delivery of the cotton tickets to the cotton company was, as expressly set forth in the trust receipt, for the purpose of securing "delivery of the shipments and secure outbound documents therefor." In other words, the cotton company, in order to sell the cotton so purchased, required delivery to itself of the cotton tickets to the end that the cotton purchased might be graded and allotted for sale. It appears from the testimony [page 407] that in the practical operation of buying and selling cotton it was necessary that the warehouse tickets covering various purchases should be gathered together in order that the cotton so purchased might be classed as to grade and quality before sale was made thereof. This plan of securing a delivery of the warehouse receipts or compress tickets covering cotton purchased and the substitution of trust receipts appears to be in accordance with the general mode of handling the cotton business. [See testimony of Mr. Norsworthy, page 421, and Mr. West, page 341.]

This plan of securing delivery to itself of the cotton tickets held by the bank, and the substitution of trust receipts therefor, was in accordance with the plan approved by the cotton company and by the bank [See letter Sept. 8, 1919, page 212, and testi-

mony of L. C. Ivy, page 215], and was known to and approved of by McDevitt, president of the cotton company [page 273], and by T. J. West, treasurer [pages 341-344]; and was the method in customary use in the buying and selling of cotton.

Thereafter and from time to time, in the conduct of its general business the cotton company sold the cotton covered by the warehouse receipts received from the bank and thereupon it would surrender the warehouse receipts to a railway company and receive bill of lading covering the cotton represented by the surrendered warehouse receipts. The cotton company would then attach the bill of lading to a draft covering the sale price of the cotton, which draft, together with the bill of lading attached, was then deposited by the cotton company to its credit as a cash item in its general checking account at the plaintiff bank. Before depositing the outbound draft with bill of lading attached as a cash item, that is, an item for which the cotton company would receive immediate credit from plaintiff bank, the cotton company would secure the written approval on said draft by some one of the vice-presidents of plaintiff bank. From time to time the cotton company, when moneys were available in its general checking account, would draw checks in favor of the plaintiff bank covering one or more of the acceptances held by the bank as bills receivable due from the cotton company, and would secure a surrender of the acceptance, together with the trust receipt attached thereto. The foregoing is the general plan of operation as carried on between the cotton

company and the plaintiff bank during the whole period of its operations, to-wit, from September, 1919, to May of 1921.

The cotton business is divided into seasons and it is not disputed that the first season of the cotton company's business began in the fall of 1919 and ended in May of 1920, and the second season began in November of 1920 and continued on through to the time of Sears' death in May, 1921. During the first season the cotton company purchased cotton in excess of ninety-five dollars, and drafts aggregating 76 in number covering the purchase price thereof were drawn upon the cotton company through the plaintiff bank, to which drafts were attached the warehouse tickets representing the cotton purchased and all said drafts after being accepted by the cotton company were paid by plaintiff bank. It is not disputed that during the first season all of the warehouse receipts attached to the 76 drafts were withdrawn by the cotton company and trust receipts substituted [page 372]. It is also not disputed that all of the cotton for which trust receipts were issued to plaintiff bank during the first season was sold and the "outbound documents," that is, the drafts with bills of lading attached covering cotton sold, was deposited as a cash item in the checking account of the cotton company in plaintiff bank, and that from time to time and at irregular intervals the cotton company drew checks upon its checking account in favor of plaintiff bank in payment of the acceptances held by the plaintiff bank, and that in no single instance



were the "outbound documents" ever deposited or returned to the collection department of plaintiff bank, and at no time was any of the acceptances or trust receipts held by the plaintiff bank, paid and discharged by the surrender direct to the collection department of plaintiff bank of the "outbound documents," but instead during the whole period of the company's operations all acceptances with trust receipts attached thereto that were paid, aggregating in all in excess of one million dollars, were paid by checks drawn by the cotton company on its general checking account in plaintiff's bank. This plan of handling payments of acceptances and securing redelivery of trust receipts by the sale of the cotton and the drawing of checks on the general checking account was known to and approved of by both the plaintiff bank and the other officers of the cotton company. [See stipulation, p. 352, and testimony of Mr. McDevitt, p. 275, and of Mr. West, p. 343.] During the first year the cotton market was a rising one, the price increasing gradually from 14¢ per pound in the fall of 1919, to as high as 40¢ per pound in the spring of 1920. During the first year the cotton company, on the purchase and sale of cotton made a very substantial profit and was able to take care of all operating expenses and pay for all cotton purchased by it through the plaintiff bank. Consequently no difficulties arose.

The second season of the cotton company's operations began in November, 1920, at which time the cotton market was on the decline, and between that date and May of 1921, when the cotton company ceased



operations, cotton gradually decreased in price from the maximum of 40¢ per pound, to as low as 8¢ per pound [page 342]. An audit of the cotton company's purchase and sales account during the second season shows that on the average every bale of cotton purchased was sold at a price of twelve dollars less than the purchase price thereof. During the second season the same plan of operation as regards purchase and sale of cotton obtained as during the first season, that is, the plaintiff bank paid for the cotton as purchased holding the acceptances of the cotton company with the warehouse receipts as security; the bank then surrendered the warehouse receipts and accepted trust receipts in lieu thereof; then the cotton company sold the cotton and deposited the "outbound documents" in its general checking account and, so far as funds were available, drew checks from time to time at irregular intervals on its checking account and paid off certain of the acceptances held by the plaintiff bank. Each time an acceptance was paid the trust receipt attached thereto was surrendered by the bank.

During the second season of the cotton company's operations the plaintiff bank handled and paid for the cotton company 162 drafts aggregating a total of approximately two hundred thousand dollars, and during the period from November 17, 1920, to May 3, 1921, it held at one time or another said 162 drafts accepted by the cotton company with trust receipts attached thereto, all of the warehouse receipts having been surrendered to the cotton company at the time the trust receipts were given. Each time a check was drawn

by the cotton company on its general checking account in favor of the bank, it was applied in payment of the oldest acceptance held by the bank. It is not disputed that the cotton company paid 76 of the acceptances held by the plaintiff bank and secured a surrender thereof, together with the trust receipt attached thereto [page 433]. It is not disputed that the cotton company sold all of the cotton for which trust receipts were given to the plaintiff bank [page 441], and that all of the "outbound documents" covering every single bale of cotton sold and covered by the trust receipt held by the plaintiff bank, were deposited as a cash item in the checking account of the cotton company in plaintiff's bank [page 441], with the exception of 385 warehouse receipts which were still on hand in the safe of the cotton company at the time of Mr. Sears' death. At the time of Sears' death the plaintiff bank was holding 87 unpaid acceptances aggregating the face value of \$82,487.96, to which were attached trust receipts calling for 1476 warehouse receipts for 1476 bales of cotton. As stated above, 385 of these warehouse receipts were later surrendered to the plaintiff bank, the remaining 1091 representing that number of bales of cotton, the original cost price of which was \$60,628.72, had been sold by the cotton company, and the "outbound documents" therefor deposited as a cash item in the general checking account of the cotton company. Out of this general checking account the cotton company had paid its general operating expenses, as well as making payments from time to time on the acceptances held by the plaintiff bank.

As a result of the steady decline in the cotton market and the fact that the cotton company sold cotton purchased during the second season at a price averaging \$12.00 per bale less than the actual cost thereof, the assets of the cotton company were depleted with the net result that at the time of Sears' death there was no money on hand with which to pay the unpaid acceptances at the bank, and the bank was left holding the 87 unpaid acceptances with trust receipts attached thereto covering 1476 bales of cotton; three hundred eighty-five warehouse receipts were later returned leaving 1091 undelivered.

It is stipulated by plaintiff bank and pleaded in its complaint that so far as the first cause of action is concerned all of the property of the cotton company was used by J. B. Sears for the purposes of the cotton company [page 376]; and it is not contended that any of the 1091 warehouse receipts for which the plaintiff bank held unredeemed trust receipts, or any of the proceeds from the sale thereof, were used by J. B. Sears personally or by any other person other than by the cotton company [page 377]. It is contended, however, that J. B. Sears, acting as secretary of the cotton company, did by his acts deceive and defraud the plaintiff bank in that he secured the delivery to the cotton company of the 1091 warehouse receipts with intent to convert to the cotton company's use; that he sold the cotton represented thereby, and failed to apply all the proceeds from the sale of such cotton, that is, the "outbound documents" to the payment of the acceptances and the discharge of the



trust receipts, but used same in general operation of the cotton company, and that as a result of such acts the 1091 bales of cotton covered by the unredeemed trust receipts were converted to the cotton company's use and were wholly lost to the plaintiff bank; and finally that the cotton company being "responsible" to the plaintiff bank for the cotton tickets so converted, a loss (to the extent of the cotton company's liability for such wrongful conversion) was sustained and that such loss was within the provision of the bond sued upon. The bond provides that the bonding company would "reimburse the employer (cotton company) for any loss not exceeding \$50,000.00 of money, securities or other personal property (including that for which the employer may be responsible to others) which the employer shall have sustained by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication on the part of the employee, while in the performance of his duties as secretary in the service of said employer and, occurring during the continuance of this bond."

During the first year the cotton company was owned by T. J. West. Later the ownership and control passed to J. B. Sears.

As stated by the learned judge of the District Court in his opinion [page 169]:

"The cotton company was, from the date of its organization and until West transferred his interest therein, a business medium only used primarily for the benefit of West. West and Sears



were experienced cotton brokers. West was conducting a cotton brokerage business at Calexico, California, and Sears had come to Los Angeles after having been connected for a number of years with a large cotton brokerage concern in the south. West expected to and did devote his main energies to his business at Calexico, where he resided, which place was at the center of the cotton growing country of Southern California and Northern Mexico. Desiring to establish a Los Angeles cotton brokerage house, West and Sears, with the active assistance of McDevitt, organized the cotton company. West paid into the treasury of the company all of the money that was contributed in exchange for stock. There was some intimation that some others of the persons named as stockholders had contributed money or services, but as to whether that was the fact is doubtful. At any rate, it was quite clearly made to appear that the issuance of stock to all persons except West and Sears was for the particular purpose of qualifying them to act as directors. The stock certificates for one share each to McDevitt, Conduit and Hartke, remained undetached from the stock book, and so remained at the time of the trial."

Before the beginning of the second cotton season, that is, in the spring of 1920, West testified [page 393] that he decided to close out the cotton company's business and was then importuned by Sears to permit him to take over the business. Accordingly some time during the fall of 1920 (the date being first fixed by the trial court as September 1st, 1920, but later changed to December 1st, 1920) West sold and trans-

ferred to J. B. Sears the 496 shares of stock of the cotton company owned by West and at all times thereafter Sears was the owner of all said stock, and the cotton company was as found by the trial court [finding No. 21], from the date of the transfer by West to Sears of said capital stock, a corporation sole—to-wit, J. B. Sears. As stated in the opinion of the learned trial judge [page 177]:

“We then must consider that from that date West owned no further interest in the business and that Sears then became the sole proprietor of it. Therefore, if there exists any liability on the part of the insurer under the bond sued upon, it must be such only as accrued prior to the first of September, 1920.” (This date was later changed to December 1st, 1920.)

There was considerable testimony as regards the exact date when the transfer of stock from West to Sears was completed, the details of which will be discussed later herein.

The judgment rendered by the trial court in the principal sum of \$24,321.97 represents the amount paid by the plaintiff bank for the cotton represented by the warehouse receipts surrendered to the cotton company prior to December 1st, 1920, and which were converted to the use of the cotton company instead of being returned to the bank.

It is urged by the bonding company (plaintiff in error) that the rights of plaintiff bank, as assignee of the cotton company, are no greater than the rights

of the cotton company so far as liability of the bonding company is concerned, and that

(a) While property of the plaintiff bank may have (as to the bank) been wrongfully converted or wilfully misapplied by the cotton company through the acts of J. B. Sears, its secretary, and by reason thereof the cotton company became liable to the bank for the financial loss it sustained, nevertheless the cotton company itself sustained no loss because it, the cotton company, received and used for its own purposes the very property belonging to the bank and which it is claimed was converted or misapplied.

(b) That if any cause of action existed in favor of the cotton company against the bonding company by reason of the loss (liability to the bank) sustained through the wrongful acts of J. B. Sears, its secretary, such cause of action ceased to exist when and as soon as the cotton company became a corporation sole—to-wit, J. B. Sears. It is not disputed that the assignment by the cotton company to the plaintiff bank of its cause of action, if any, on the bond was made after the cotton company became a corporation sole—to-wit, J. B. Sears.

At the time the bond in question was applied for the cotton company entered into certain promissory warranties with the bonding company, the strict performance of which was a condition precedent to liability on the bond. The plaintiff in error urges the breach by the cotton company of certain of these promissory warranties and particularly the failure on the part of the cotton company to have its books and accounts



audited and checked by T. J. West, as provided in the application for the bond.

It is also urged by plaintiff in error that the cotton company failed to notify the bonding company of its alleged loss within the time provided in the bond, and that such failure relieved the bonding company of liability.

### Opinion of Trial Court.

The learned trial judge at the conclusion of the trial rendered a written opinion [page 168] and later two memorandum supplemental opinions [pages 181 and 183] wherein he discusses at considerable length the facts in the case. In substance the trial court in his opinion holds:

(a) That the cotton company was from its organization to the date of the transfer of stock by West to Sears, a business medium only through which West conducted his cotton brokerage business [page 169], and that the other four officers and directors were “dummy” directors, it appearing that one share of stock was issued to J. B. Sears, the remaining three shares, while made out in the name of the other directors were never removed from the stock certificate book.

(b) That about September 1st, 1920 (which date was later changed to December 1st, 1920), West turned over the ownership and control of the cotton company to Sears and from and after that date the cotton company was a corporation sole—to-wit, J. B. Sears. In its opinion [page 176] the trial court points



out that for the purpose of determining liability upon the bond, the question of transfer of the corporation from West to Sears should be considered in the light of *transfer of control* rather than exact date of the *transfer of the stock* certificates themselves. The portion of the opinion referred to is as follows:

“Considering next the evidence as to the transfer of West’s stock to Sears, and its effect upon the liability of the defendant: Remembering that, as has been already observed, the questions here are to be considered as though the cotton company was the plaintiff, the evidence of West, who was the owner of the cotton company, as to when he transferred his interest to Sears, must be allowed full weight. A different consideration might arise, were this an action by a creditor to enforce a stockholder’s liability for corporate debts against West. If West, being the company, declares to the defendant: ‘This corporation went under the ownership of Sears at a certain date, and Sears then came into full complete control’ he would announce such a change in the conditions as to make the hazard different from that existing when the insurer made its bond. Furthermore, public policy would not favor the enforcement of a contract which would permit an individual to indemnify himself against his own misconduct.

“West testified that he made the sale of his stock to Sears during the latter part of August. He contended also that it was a part of the agreement of sale that the transfer should be considered as relating back to the month of May, 1920, but I think, the evidence on the subject being considered altogether, the best conclusion that can be made is to fix the date of the transfer at the first of September, 1920. We then must consider that from that date West owned no further interest in the business, and that Sears

then became the sole proprietor of it. Therefore, if there exists any liability on the part of the insurer under the bond sued upon, it must be such only as accrued prior to the first of September, 1920."

(c) That the first year of the cotton company's operations ending about May, 1920, was a good year and a considerable profit was made on the purchase and sale of cotton; that the second season, beginning in the fall of 1920, was a bad season, and that the purchase and sales accounts show a loss in a large amount.

(d) That pursuant to the arrangement made between the cotton company and the bank, as detailed in letter dated September 8, 1919 [page 178], Sears, as secretary of the cotton company, secured delivery to the cotton company of a large number of warehouse tickets substituting trust receipts; that during the second year on account of loss arising from sale of cotton at less than cost the cotton company became "hopelessly involved and owed the bank a sum considerably in excess of \$50,000.00, which was wholly unsecured." That a later check showed that a large number of warehouse receipts, for which the plaintiff bank held trust receipts, had been sold by the cotton company and the proceeds used in its business for the payment of operating loss of the cotton company.

(e) That the acts of Sears, as secretary of the cotton company, in failing to return "outbound documents" covering the sale of cotton for which the plaintiff bank held trust receipts, was a breach of faith; the court says [page 179]:

“it approached an embezzlement of collateral in which the bank held a qualified property interest \* \* \* and the unauthorized use of the securities by Sears should be held to amount to a wilful misapplication of property for which the cotton company was responsible to the bank. Sears’ breach of faith did result in a loss to the cotton company, because it would add to its liabilities the value of the collateral illegally withheld by Sears and used without authority in the business.”

(f) That the fact that the property in which the bank held a qualified property interest and for which the cotton company was responsible, was received by, and the proceeds from the sale thereof devoted to the business of the cotton company, and not appropriated by Sears to his own use or to the use of any other person than the cotton company, was not a good defense for the reason that by reason of the misapplication of the property in which the bank had an interest, that is, the cotton tickets covered by the trust receipts, the cotton company became liable to the bank for the value thereof.

(g) That the liability of the cotton company to the plaintiff bank for the securities so misapplied to the cotton company’s use by Sears as its secretary, constituted a loss to the cotton company, for which the bonding company is liable, but the court limits the extent of that liability to the amount of liability incurred prior to the date when the cotton company became a corporation sole, to-wit, J. B. Sears.



## THE BILL OF EXCEPTIONS.

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The Facts and Circumstances Surrounding the Preparation, Service, Proposing of Amendments and Settling of the Bill of Exceptions Were Sufficient to Justify the Trial Court in Allowing and Settling the Bill of Exceptions After the Term During Which the Judgment Was Rendered, and the Defendant in Error Is Estopped to Urge That the Settlement of the Bill of Exceptions After the Term Was Error. The Bill of Exceptions Should Be Considered a Part of the Record.

Upon the presentation for settlement of the bill of exceptions in the lower court objection was made that it had not been presented to the learned judge below for settlement and signing, nor was the same settled and signed, within the time allowed by law, or within the term of the court at which the judgment was rendered and entered. Since this objection will doubtless be renewed here we desire to state the reasons which, in our judgment, justified the trial court in settling and signing the bill of exceptions and ordering that it be made a part of the record herein.

The relevant facts, all of which appear in the affidavit of Dale H. Parke [pages 483-493] and which are not disputed by the affidavit filed by counsel for defendant in error, are as follows:

Judgment was entered on the 7th day of March, 1925; by stipulation of counsel and order of court,



the time within which defendant might prepare, serve and file its bill of exceptions was regularly and in good time extended to and including the 15th day of June, 1925 [pages 514-517]; the proposed bill of exceptions was duly served and filed on June 10, 1925. It then became the duty of the plaintiff below to prepare and present its proposed amendments and with this object in view and at plaintiff's request, a stipulation [page 518] was entered into extending plaintiff's time to prepare, serve and file its proposed amendments until the 9th day of July, 1925. The term of court during which the judgment was entered expired at midnight on July 12, 1925. On the afternoon of July 8th, plaintiff served and filed "Proposed Amendments to the Bill of Exceptions" which said proposed amendments contained 296 proposed amendments covering 59 typewritten pages; that upon receipt of the proposed amendments, counsel for defendant communicated by telephone with counsel for plaintiff to arrange, if possible, for a conference with a view of agreeing upon the proposed amendments, and thereupon counsel for plaintiff stated to counsel for defendant:

"That the proposed amendments were prepared by two young men in our office during my absence and they may have been over cautious, and I suggest that you check the proposed amendments, indicating those you think are proper and those you think ought not to be allowed and return your copy of the proposed amendments with your notations thereon and I will check them over within the next few days and let you know which ones we will insist upon."

That pursuant to said request counsel for defendant checked the proposed amendments, the time for checking same requiring several days, and did on the 15th day of July, 1925, return, at request of counsel for plaintiff the copy of proposed amendments theretofore served upon defendant, with notations thereon as to the proposed amendments which the defendant would consent to. The returned copy of the proposed amendments was accompanied by letter dated July 15, 1925 [page 486]; that thereafter and between July 15, 1925, and July 22, 1925, counsel for defendant called one of the counsel for plaintiff on two occasions by telephone and was advised that the proposed amendments were being rechecked by plaintiff's counsel and would be ready for resubmission within a day or two; that on July 22, 1925, plaintiff's counsel resubmitted its proposed amendments, having stricken out a large number of the amendments originally proposed, and adding some new ones. The new set of proposed amendments was accompanied by letter written by plaintiff's counsel [page 488]; that the new proposed amendments were not received by counsel for defendant until late in the afternoon of July 22d, and on the morning of July 23d, one of the counsel for plaintiff called counsel for defendant and requested that a conference be held with a view of agreeing upon the amendments as then proposed, and to that end counsel for plaintiff and defendant devoted a substantial portion of July 23d and 24th in going over the proposed amendments and an agreement was had on substantially all amendments proposed; that at the time the original bill of exceptions was served certain

exhibits were omitted and counsel for plaintiff agreed at that time to indicate what portions of such exhibits they desired printed in the record, which information was not furnished to counsel for defendant until the 25th day of July, 1925. The particular exhibits to which reference is made were the minutes of the cotton company and certain auditor's reports. There was not sufficient time between the 8th day of July, 1925, when the original set of proposed amendments were served on counsel for defendant, and Saturday night, July 11th, (the term expiring on Sunday night) within which the proposed amendments might have been made had they been approved of by counsel for defendant as the amendments originally proposed required a rewriting of substantially the whole bill; that counsel for defendant relied upon the request of counsel for plaintiff that the proposed amendments as originally served be returned for correction by plaintiff's counsel, and upon the conduct of counsel for plaintiff, as set forth in the affidavit of Dale H. Parke above referred to. That a final agreement between counsel as to all the proposed amendments was not arrived at until Saturday, July 25th. Whereupon, a public stenographer was employed and not less than two full days was required to rewrite the proposed bill in accordance with the amendments agreed upon. That of the amendments originally proposed by plaintiff approximately 121 were later by agreement of plaintiff's counsel waived. Upon due notice, the bill of exceptions as rewritten in accordance with the proposed amendments as agreed upon between counsel was on the 28th



day of July, 1925, presented to the court for settlement and allowance. Objections were made to the settlement on the grounds that the court was without authority to settle the bill of exceptions, the term of court during which judgment was rendered having expired, and the legal question involved was heard. Whereupon the trial court signed and settled the bill of exceptions and entered an order making said bill of exceptions a part of the record herein. [Page 509.]

While it is the general rule that the bill of exceptions must be signed and settled within the term of court during which the judgment is entered, such rule is not *jurisdictional*. The court has power in its discretion, where facts justify the exercise of such discretion, to settle the bill after the term. This rule is recognized by a long line of cases, some of which have been decided by this court.

Pacific Bank v. Hanna, 90 Fed. 76;

Sutherland v. Pearce, 186 Fed. 783.

That the settling of the bill of exceptions within the term is not jurisdictional is recognized by a great many United States Supreme Court decisions, beginning with:

United States v. Breitling, 20 Howard 253—  
15 L. Ed., page 900.

See also

Hume v. Bowie, 148 U. S. 245-253—37 L. Ed.  
438.

In the foregoing cases the courts hold that if a bill is filed within the term the settlement thereof



may, where circumstances warrant, be made after the expiration of the term. See also

Koewing v. Wilder, 126 Fed. 473;

Harrison v. German American Fire Ins. Co.,  
90 Fed. 758.

Under the circumstances as detailed in the record. [pages 483 to 520], and in view of the stipulations and conduct of counsel for plaintiff, the plaintiff is estopped from objecting to the settlement of the bill of exceptions after the expiration of the term.

*Re Chateaugay Ore & Iron Co.*, 128 U. S. 544—  
32 L. Ed. 508;

*Du Pont etc. v. Smith*, 249 Fed. 403.

Counsel for plaintiff urged to the trial court that the writ of error having been granted and citation issued prior to the presentation of the bill of exceptions but before the cause had been docketed and record filed in the appellate court, the trial court was without jurisdiction to settle the bill.

On this point we respectfully submit the following authorities which hold in accordance with the law as stated in *Foster on Federal Practice*, 5th Edition, Volume 3, page 1594, as follows:

“A bill of exceptions if otherwise in time may be signed after a writ of error has been sued out, or an appeal allowed and citation issued, or a supersedeas bond filed and approved.”

*Hunnicutt v. Peyton*, 102 U. S. 333, 357—26  
L. Ed. 113, 117;

*Davis v. Patrick*, 122 U. S. 138, 30 L. Ed.  
1090;

*Cook v. Klonos*, 164 Fed. 529 (9th Circuit);  
*Ulmer v. U. S.*, 266 Fed. 176.

We respectfully submit that the trial court was justified in settling and allowing the bill of exceptions and that the enforcement of the common law rule that the bill should be settled within the term should not be enforced so rigidly that it will work injustice, and particularly in a case where, as in the present case, counsel for defendant was not at fault and the conduct of counsel for plaintiff was such as should estop plaintiff from urging that the bill of exceptions be not settled. As stated by the learned trial judge in the order settling the bill of exceptions [page 510]: “between the said 9th day of July, 1925, and the date of this order negotiations toward an agreement between counsel, covering the proposed amendments, were pending and said proposed amendments were not finally agreed upon between the parties until the 25th day of July, 1925.”

After full consideration the trial court considered that good cause existed for the settlement of the bill of exceptions and the ends of justice will be better served by having the bill of exceptions considered as a part of the record.

**Motion for Non-Suit and Motion for Judgment in Favor of Defendant and Special Findings in Favor of Defendant Were Requested in the Trial Court.**

At the conclusion of plaintiff's testimony, the defendant moved for a non-suit [page 377]. Said motion was based upon the following grounds:

(a) That there was not sufficient evidence to warrant a finding of fact by the trial court that the cotton company had sustained any loss within the meaning of the bond sued upon, it appearing affirmatively from the testimony introduced by plaintiff that all money and property received by Sears and which came into his hands in trust as an employee of the cotton company, was fully accounted for and applied to the use and business of the cotton company.

(b) That there was no evidence to support any finding of fact as to the value of the securities—to-wit, warehouse receipts or cotton tickets which plaintiff claims were misapplied by J. B. Sears and for which misapplication the cotton company was liable to the plaintiff bank.

(c) That it affirmatively appeared from the testimony introduced in evidence by the plaintiff that the cotton company failed to comply with the promissory warranty regarding the auditing and inspecting of the books by T. J. West in that the cotton company failed to have the books, accounts, stocks and securities inspected, audited and approved each month by T. J. West.

At the conclusion of the taking of testimony the defendant made request of the trial court for special findings of fact on the issues [page 467] and also presented to the trial court a motion that the court enter findings and judgment in favor of the defendant upon the following grounds, among others, [pages 462-466]:

(a) That the first cause of action in plaintiff's complaint as amended does not state facts sufficient to constitute a cause of action.

(b) That the evidence is insufficient in that there is no evidence that J. B. Sears converted to his own use or to the use of any person, partnership or corporation any of the money, property, rights or credits of the cotton company, other than to the use of the cotton company.

(c) That the evidence is insufficient in that there is no evidence legally sufficient to show that the cotton company sustained any loss by reason of any of the wrongful acts of J. B. Sears while in the performance of his duties as secretary.

(d) That the evidence shows that the cotton company at all times knew of the acts being performed by J. B. Sears and which it is alleged were wrongful and caused the loss sought to be recovered, and that the cotton company failed to notify the bonding company within the time expressly provided in the bond of such act or acts so done and performed by J. B. Sears.

(e) For the reason that the evidence shows that the cotton company failed to have its books, accounts, stocks and securities inspected, audited and verified with funds on hand or in the bank each month by T. J. West, treasurer, as required under the bond and application made in connection therewith.

(f) That the evidence shows that during all the period of time, in which the alleged wrongful acts of



J. B. Sears were performed and which it is claimed resulted in a loss to the cotton company, the said J. B. Sears was the owner of all the capital stock of the cotton company and said cotton company was in fact a corporation sole—to-wit, J. B. Sears; and that at all times after the transfer by T. J. West to J. B. Sears of his stock interest said cotton company was a corporation sole—to-wit, J. B. Sears, and, therefore, the cotton company could not recover from the bonding company for any alleged loss since to do so would be to permit the said J. B. Sears to recover for a loss resulting from his own wrongful acts.

**The Motions and Request for Special Findings of Fact Were by the Trial Court Denied and Exceptions Thereto Allowed. (Page 117.)**

### **Assignments of Error.**

Now comes the above named defendant, plaintiff in error herein, and says that in the record and proceedings in the above entitled action there is manifest error, and now makes, presents and files the following assignments of error upon which it will rely, as follows, to-wit:

#### **I.**

That the first cause of action as set forth in plaintiff's original complaint as amended by the amendments thereto does not state facts sufficient to constitute a cause of action against the defendant herein and the court erred in over-ruling defendant's demurrer thereto.

II.

The court erred in over-ruling defendant's motion for non-suit and defendant's motion that the court enter findings and judgment in favor of the defendant.

III.

The evidence received upon the trial of the above entitled action was and in wholly insufficient to justify the findings of the trial court that the California Cotton & Factorage Company sustained any loss of any kind or character by reason of any fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears while in the performance of his duties as secretary of the said California Cotton & Factorage Company.

IV.

The evidence received upon the trial of the above entitled action was and is wholly insufficient to justify the finding of the trial court as set forth in finding of fact No. VI that the said J. B. Sears applied to and secured from the plaintiff the warehouse receipts

“with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating, and wilfully misapplying said warehouse receipts, the cotton represented thereby, and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained, of thereby causing a loss to said California Cotton & Factorage Company of money, securities, and personal property for which it would be and has become responsible to the plaintiff herein.”

V.

There is no evidence to justify that part of the finding of the court No. VI insofar as the court finds that the said J. B. Sears at the time of executing the trust receipts and securing delivery to him of the warehouse receipts, or cotton tickets, made any other or different representations to the plaintiff or any of its officers than the representations set forth in the letter of September 8, 1919, written by the California Cotton & Factorage Company to the plaintiff bank, being Plaintiff's Exhibit No. 5.

VI.

There is no evidence to justify that part of finding of fact of the court No. VI wherein the court found that

“and pursuant to said fraudulent and dishonest plan and scheme said J. B. Sears at various times and irregular intervals procured from the plaintiff herein between the 19th day of November, 1920 and said 25th day of April, 1921, 1,476 warehouse receipts for 1,476 bales of cotton and issued and delivered to the plaintiff in acknowledgement thereof 87 of said trust receipts.”

for the reason that the evidence shows that the securing of said warehouse receipts for 1,476 bales of cotton and the issuance and delivery of the 87 trust receipts therefor was done and performed by said J. B. Sears with the consent and knowledge of the plaintiff and pursuant to and in strict keeping with the plan of operations entered into and agreed upon by and be-

tween the plaintiff and the California Cotton & Factorage Company as evidenced by the letter of September 8, 1919, plaintiff's Exhibit No. 5.

## VII.

There is no evidence to justify that part of finding of fact of the court No. VII to the effect that said J. B. Sears

“without the knowledge of said California Cotton & Factorage Company, or any of its officers or agents other than J. B. Sears, pursuant to said fraudulent and dishonest plan and scheme by him entertained as hereinbefore found, fraudulently and dishonestly converted, misappropriated and wilfully misapplied 1,091 of said 1,476 warehouse receipts and 1,091 bales of cotton represented thereby.”

## VIII.

There is no evidence to justify that part of finding of fact of the court No. VII that said J. B. Sears in performing the acts as set forth in said finding No. VII violated any of his duties as secretary or violated any of the promises and representations made by him to the plaintiff or that in depositing outbound drafts covering cotton sold, he, the said J. B. Sears, made any misrepresentations to the officer or officers of the plaintiff bank or caused said sight drafts to be deposited as cash items in the account of the California Cotton & Factorage Company for the purpose of defrauding or cheating the plaintiff bank or of defrauding or cheating the plaintiff or said California



Cotton & Factorage Company or of misapplying or misappropriating any of its property.

IX.

There is no evidence to support that part of the finding of fact of court No. VII that the said J. B. Sears pursuant to said alleged fraudulent scheme or otherwise or at all falsified the books and accounts of the California Cotton & Factorage Company in the manner as set forth in finding of fact No. VII or otherwise or at all and particularly that he falsified the books and accounts of the said California Cotton & Factorage Company by entering or causing to be entered therein the various amounts of money received from the sales of cotton and carrying same upon the bank pass book as monies and funds belonging entirely without limitation of any kind to the said company; or that he wilfully failed to enter in the books of said company any entry or memorandum indicating that trust receipts had been issued to the plaintiff covering the cotton that was being sold and disposed of or that he wilfully failed to make or cause to be made any entry or memorandum indicating that the monies received from the sale of cotton was charged with any trust or were in any manner monies or funds other than the absolute and unencumbered funds of the said Cotton Company.

X.

There is no evidence to support that part of finding of fact of the court No. VII that said J. B. Sears frequently represented to the California Cotton & Fac-

torage Company, its officers and directors, that the various sums of money and credits entered upon the bank pass book and books of account of the Cotton Company were the funds and monies of the said Cotton Company or to the effect that the plaintiff or said California Cotton & Factorage Company, or any of its officers and directors, relied upon or were deceived by any dishonest or false and fraudulent representations made to them by said J. B. Sears.

XI.

That there is no evidence to support or justify that part of finding of fact of the court No. VII that the 1,091 bales of cotton sold and disposed of by the Cotton Company and for which the plaintiff held trust receipts was at the time the same was sold and disposed of, of the reasonable value of \$60,594.62 or any part thereof or any sum whatsoever.

XII.

There is no evidence to support or justify that portion of finding of fact of the court No. VIII that said J. B. Sears did secure possession of the warehouse receipts held by plaintiff as collateral security by any false or fraudulent representations or that in selling and disposing of the cotton covered by trust receipts held by the plaintiff the said J. B. Sears acted in a fraudulent or dishonest manner or was guilty of any conversion, misappropriation or wilful misapplication of said warehouse receipts or of the cotton covered thereby, and that said J. B. Sears in selling and disposing of said cotton or in disbursing the

proceeds realized from the sale thereof was acting in a false or fraudulent manner or practicing any deceit upon the plaintiff or upon the California Cotton & Factorage Company.

### XIII.

There is no evidence to support or justify that part of finding of fact of the court No. VIII that said J. B. Sears

“fraudulently and dishonestly converted, misappropriated and wilfully misapplied the monies and funds placed to the credit of the said California Cotton & Factorage Company following the dishonest and fraudulent sales of cotton and disposition of warehouse receipts and bills of lading, all as herein found, by using said monies and funds for the purpose of dealing and speculating in cotton in the name of the said California Cotton & Factorage Company and conducting such dealings and speculations at a loss and paying said losses out of said monies and funds and in the payment of claims and demands incurred by said J. B. Sears in said dealings and speculations in cotton.”

### XIV.

There is no evidence to support or justify that part of the finding of fact of the court No. VIII that

“relying entirely upon said false and fraudulent representations of said J. B. Sears herein found and said deceits by him practiced upon it and them as herein found, said California Cotton & Factorage Company, its directors and officers, continued the business of said California Cotton &

Factorage Company and consented to said J. B. Sears, subsequent to said 19th day of November, 1920, continuing to act as the secretary of said company—and to continue to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith as herein found.”

XV.

There is no evidence to justify or support that portion of finding of fact of the court No. IX that the California Cotton & Factorage Company sustained any loss or has become responsible to the plaintiff herein in the sum of \$60,594.62, or any sum of money whatsoever, with interest thereon by reason of any fraud, dishonesty, wrongful abstraction and wilful misapplication of said 1,091 warehouse receipts, and/or the cotton held thereunder, and/or said bills of lading, and/or the money proceeds and credits realized from the sale thereon but on the contrary said evidence shows that said indebtedness existing in favor of the plaintiff against the California Cotton & Factorage Company was incurred pursuant to and in strict keeping with the plan of operations agreed upon between the plaintiff and the California Cotton & Factorage Company as evidenced by the letter of September 8, 1919, Plaintiff's Exhibit No. 5, and that all of the monies received from the sale of the said 1,091 bales of cotton was received by and deposited in plaintiff bank to the credit of the California Cotton & Factorage Company and no part of said cotton evidenced by said 1,091 warehouse receipts or any of the monies



realized from the sale thereof was lost to the California Cotton & Factorage Company.

XVI.

That there is no evidence to support or justify any finding by the trial court that the said J. B. Sears in securing the 1,476 warehouse receipts from the plaintiff and issuing and delivering to plaintiff in acknowledgment thereof 87 trust receipts or in selling and disposing of 1,091 bales of cotton evidenced by said warehouse receipts and covered by said trust receipts was acting pursuant to any fraudulent or dishonest intent or design on his part or in violation of any agreement or representations made by him or by the California Cotton & Factorage Company to the plaintiff in relation to said warehouse receipts and the cotton covered thereby. The evidence conclusively shows that the securing of said warehouse receipts and the issuance of trust receipts to the plaintiff was known to and approved of by the officers and directors of the plaintiff and of the California Cotton & Factorage Company.

XVII.

There is no evidence to support or justify any finding of the trial court that said J. B. Sears in depositing the "outbound documents" covering the sale of cotton for which the plaintiff bank held trust receipts as a cash item to the credit of the California Cotton & Factorage Company was acting pursuant to any fraudulent or dishonest intent or design on the part of the said J. B. Sears for the reason that on the contrary the

evidence shows that the officers and directors of the plaintiff and of the California Cotton & Factorage Company knew and approved of the handling of the sale of said cotton and the disbursement of the funds realized thereupon in the manner in which the same were handled by said J. B. Sears.

XVIII.

There is no evidence to support or justify the finding of fact of the court No. X that within ten days after the California Cotton & Factorage Company discovered the alleged loss claimed to have been sustained by it, it notified the defendant herein of said alleged loss and of the facts in connection therewith.

XIX.

There is no evidence to justify or support the finding of fact of the court Nos. XIV and XV that J. B. Sears was not allowed and permitted by the California Cotton & Factorage Company as he deemed best.

XX.

There is no evidence to support or justify that part of the finding of fact of the court No. XVI that T. J. West, treasurer of said California Cotton & Factorage Company,

“visited the office of the said California Cotton & Factorage Company semi-monthly during the term of said bond as herein found and at such times conferred with J. B. Sears respecting the business of said Company and checked over the

books of said Company but not in detail at any time examining the cotton account, being the purchase and sales cotton account, showing the cotton bought and sold and at said times examined the records disclosing the amount of cotton bought, the amount of cotton sold, the number of bales unsold, the entries respecting the hedging of the same, and also examined the cash account and the acceptance account, together with the cotton tickets indicating the number of bales of cotton on hand and compared the same and determined that they corresponded to the acceptances in the plaintiff bank and that at such times said T. J. West checked the books of said Company for the purpose of determining the amount of money owing by said Company to said Citizens National Bank and examined the statements and books of said Company and did observe the amount of cotton purchased, the number of cotton tickets and bales of cotton on hand, and examined the ledger books of said company and the various accounts therein including the cotton account, and checked the same with the bookkeeper's statement furnished at the end of each month.”;

or that

“that said T. J. West checked the accounts of said company, including the bank account, semi-monthly by said statements rendered by the bookkeeper as herein found”

or that

“that it is not true that if an audit had been made each month as provided in the contract between the California Cotton & Factorage Company and said defendant it would have revealed the facts

as herein found and that the loss herein found to have been sustained could have been checked, lessened and stopped.”

XXI.

There is no evidence to support or justify that portion of finding of fact of the court No. XVII that the California Cotton & Factorage Company or the plaintiff herein did not discover the alleged loss claimed to have been sustained by the California Cotton & Factorage Company by the alleged acts of J. B. Sears until the 19th day of May, 1921.

XXII.

There is no evidence to justify or support the finding of fact of the court No. XIX that it is not true that all of the monies of the California Cotton & Factorage Company handled by J. B. Sears were used in and for the purchase of cotton and other commodities for the Cotton Company or for the purpose of paying the expenses or costs of operation of the Cotton Company.

XXIII.

There is no evidence to support or justify that portion of finding of fact of the court No. XIX that the warranties made by the California Cotton & Factorage Company to the defendant in the application for bond were not untrue or were not broken in all or any of the respects as alleged in defendant's answer; or that the defendant is or has not been released from all or any of the obligations of liability to plaintiff



under said bond sued upon herein; or that the California Cotton & Factorage Company has not breached any of the warranties of said bond or done anything contrary to or in violation of the terms of the application for said bond.

#### XXIV.

There is no evidence to support or justify the finding of fact of the court No. XX that the alleged loss to the California Cotton & Factorage Company was not incurred with the full knowledge of the officers and directors of said Cotton Company and with their consent.

#### XXV.

There is no evidence to justify or support that portion of the finding of fact of the court No. XXI that the sale and transfer by T. J. West of 496 shares of stock to said J. B. Sears occurred on the 1st day of December, 1920, or at any date subsequent to the 17th day of November, 1920; or that it was only on and after December 1, 1920, that J. B. Sears became and was the practical owner of the entire assets and business of said Cotton Company.

#### XXVI.

There is no evidence to support or justify that part of the finding of fact of the court No. XXIV that the 455 bales of cotton covered by sight drafts accepted by the plaintiff prior to December 1, 1921, were at the time the same were disposed of by J. B. Sears had the reasonable value of \$29,337.99 or any part thereof or any sum whatsoever.

XXVII.

That the court erred in its conclusions of law in finding that the plaintiff is entitled to judgment against the defendant on its first cause of action in the sum of \$24,321.97, together with interest thereon or any sum whatsoever.

XXVIII.

That the court erred in giving, making, rendering, and filing its judgment in the above-entitled action in favor of the plaintiff and against the defendant in this, that said final judgment was and is contrary to law and to the cause made and facts stated in the pleadings and records in said action.

XXIX.

That the court erred in failing and refusing to make findings of fact herein in accordance with the "Request for Special Findings of Fact" as made by the defendant to the trial court prior to the submission of said case for the court's decision, and which "Request for Special Findings" is set forth in the transcript of the record herein.

XXX.

That the court erred in failing to find as a fact that T. J. West sold and transferred to J. B. Sears 496 shares of the capital stock of the California Cotton & Factorage Company on or prior to the 17th day of November, 1920, and that at all times on and after November 17, 1920, said California Cotton & Factorage Company was a corporation sole, to-wit, J. B.

Sears, and under his exclusive management and control.

XXXI.

That the court erred in failing to find as a fact that the said California Cotton & Factorage Company failed to do and perform those promises and warranties set forth in the application for bond made by said California Cotton & Factorage Company to defendant in that the said California Cotton & Factorage Company did not by and through its treasurer, T. J. West, cause the books and records of said California Cotton & Factorage Company to be inspected and audited and verified with funds on hand or in bank as expressly provided for in paragraph 12 of the application made by the said California Cotton & Factorage Company to the defendant for said bond.

In order that the foregoing assignments of error may appear of record said defendant presents the same to said court and prays that such disposition be made thereof as is in accordance with law and the statutes of the United States in such cases made and provided; and said defendant, plaintiff in error herein, prays the reversal of the above mentioned final judgment heretofore given, made, rendered, entered and filed in the above entitled court in the above-entitled action.

## POINTS OF PLAINTIFF IN ERROR.

### I.

THE COTTON COMPANY SUSTAINED NO LOSS BY REASON OF THE ALLEGED ACTS OF J. B. SEARS, ITS SECRETARY, IN WRONGFULLY CONVERTING OR WILFULLY MISAPPLYING THE 1091 WAREHOUSE TICKETS OR THE COTTON REPRESENTED THEREBY AND WHICH WERE COVERED BY UNREDEEMED TRUST RECEIPTS HELD BY PLAINTIFF BANK, AND THE COURT ERRED IN FINDING THAT ANY SUCH LOSS WAS INCURRED BY THE COTTON COMPANY.

ASSIGNMENTS OF ERROR NOS. 1, 2, 3, 15, 22, 27, 28 AND 29.

### II.

THE FIRST CAUSE OF ACTION OF PLAINTIFF'S COMPLAINT AS AMENDED DOES NOT STATE FACTS SUFFICIENT TO CONSTITUTE A CAUSE OF ACTION AGAINST DEFENDANT BONDING COMPANY, AND THE TRIAL COURT ERRED IN OVERRULING DEFENDANT'S DEMURRER THERETO AND IN REFUSING TO FIND JUDGMENT FOR THE DEFENDANT.

ASSIGNMENTS OF ERROR NOS. 1 AND 2.

### III.

THERE IS NO EVIDENCE TO SUPPORT OR JUSTIFY THE FINDINGS OF THE TRIAL COURT AS SET FORTH IN FINDINGS No. VII THAT THE REASONABLE VALUE OF THE 1091 BALES OF COTTON SOLD AND DISPOSED OF BY THE COTTON COMPANY AND FOR WHICH THE PLAINTIFF BANK HELD TRUST RECEIPTS, WAS AT THE TIME THE SAME WERE SOLD AND DISPOSED OF, OF THE REASONABLE



VALUE OF \$60,594.62; OR TO SUPPORT FINDING No. XXIV THAT THE 455 BALES OF COTTON COVERED BY WAREHOUSE RECEIPTS DELIVERED BY PLAINTIFF BANK TO THE COTTON COMPANY PRIOR TO DECEMBER 1ST, 1920, AND NOT RETURNED TO THE BANK WERE AT THE TIME THEY WERE SOLD AND DISPOSED OF, OF THE REASONABLE VALUE OF \$29,336.99.

ASSIGNMENTS OF ERROR NOS. 11 AND 26.

#### IV.

THE COTTON COMPANY DURING THE LATTER PART OF 1920 BECAME A CORPORATE SOLE—TO-WIT, J. B. SEARS, AND THEREAFTER J. B. SEARS, THE “RISK” NAMED IN THE BOND, WAS IN COMPLETE OWNERSHIP AND CONTROL OF THE COTTON COMPANY. THAT ON AND AFTER THE DATE WHEN SUCH COMPLETE OWNERSHIP AND CONTROL WAS OBTAINED BY J. B. SEARS THE COTTON COMPANY—TO-WIT, J. B. SEARS, HAD NO RIGHT OF ACTION TO RECOVER FOR ANY LOSS SUSTAINED BY THE WRONGFUL ACTS OF J. B. SEARS, WHETHER COMMITTED PRIOR TO OR SUBSEQUENT TO THE DATE ON WHICH THE OWNERSHIP AND CONTROL OF THE COTTON COMPANY WAS ACQUIRED BY SEARS. FOR THAT REASON THE TRIAL COURT ERRED IN FINDING JUDGMENT FOR PLAINTIFF AND IN REFUSING TO GRANT DEFENDANT’S MOTION FOR JUDGMENT FOR DEFENDANT. IN VIEW OF THE FINDING OF FACT THAT THE COTTON COMPANY BECAME A CORPORATION SOLE—TO-WIT, J. B. SEARS, ON DECEMBER 1ST, 1920, THE TRIAL COURT ERRED IN ITS CONCLUSIONS OF LAW THAT THE PLAINTIFF (ASSIGNEE FOR COLLECTION OF THE COTTON COMPANY) WAS ENTITLED

TO JUDGMENT FOR ANY LOSS RESULTING FROM THE WRONGFUL ACTS OF J. B. SEARS.

ASSIGNMENTS OF ERROR NOS. 2, 25, 27, 28 AND 30.

V.

THE COURT ERRED IN ITS FINDING OF FACT THAT THE CONTROL OF THE COTTON COMPANY DID NOT PASS FROM WEST TO SEARS UNTIL DECEMBER 1ST, 1920.

ASSIGNMENTS OF ERROR NOS. 25 AND 30.

VI.

THERE WAS A BREACH BY THE COTTON COMPANY OF THE PROMISSORY WARRANTIES MADE TO THE BONDING COMPANY AND GIVEN AS CONSIDERATION FOR THE EXECUTION OF THE BOND, AND OF THE PROVISIONS OF THE BOND IN THAT THE COTTON COMPANY'S BOOKS, ACCOUNTS, STOCK AND SECURITIES WERE NOT INSPECTED AND AUDITED BY T. J. WEST, AS WARRANTED.

ASSIGNMENTS OF ERROR NOS. 31, 27, 28, 23, 20 AND 2.

VII.

THE COTTON COMPANY HAD KNOWLEDGE OF THE PERFORMANCE BY SEARS OF THE ACTS DONE BY HIM AS SECRETARY AND WHICH IT IS NOW CLAIMED WERE DISHONEST, FOR THE REASON THAT THE ACTS DONE BY SEARS AS EXPRESSLY PLEADED BY PLAINTIFF, WERE WITHIN THE SCOPE OF HIS DUTIES AS SECRETARY AND WERE FOR THE EXCLUSIVE BENEFIT OF THE COTTON COMPANY IN THE PROSECUTION OF THE BUSINESS FOR WHICH IT WAS INCORPORATED. IT IS NOT CLAIMED

THAT SEARS SOUGHT TO GAIN ANY PERSONAL ADVANTAGE OR BENEFIT TO HIMSELF OR TO ANY OTHER PERSON THAN THE COTTON COMPANY.

THE FAILURE OF THE COTTON COMPANY, HAVING KNOWLEDGE OF THE ACTS OF SEARS NOW COMPLAINED OF, TO NOTIFY THE BONDING COMPANY THEREOF WITHIN THE TIME PROVIDED IN THE BOND, PREVENTS ANY RIGHT OR RECOVERY THEREON AND ESTOPS THE COTTON COMPANY FROM MAINTAINING ANY ACTION PREDICATED UPON THE ALLEGED FRAUDULENT ACTS. IN VIEW OF THIS KNOWLEDGE ON THE PART OF THE COTTON COMPANY IT WAS ERROR FOR THE TRIAL COURT TO FIND THAT ANY FRAUD OR DECEIT WAS PRACTICED BY SEARS UPON THE COTTON COMPANY.

ASSIGNMENTS OF ERROR NOS. 18, 21, 24, AND 4 TO 17 INCLUSIVE.

A large number of the foregoing points touch upon the same subject matter and a portion of the facts, argument and law given in support of one point applies also to other points and should be considered therewith. The foregoing points are a general statement of the issues of fact and law involved and all assignments of error which relate to the same general issue are considered together.

I.

The Cotton Company Sustained No Loss by Reason of the Alleged Acts of J. B. Sears, Its Secretary, in Wrongfully Converting or Wilfully Misapplying the 1091 Warehouse Tickets or the Cotton Represented Thereby and Which Were Covered by Unredeemed Trust Receipts Held by Plaintiff Bank, and the Court Erred in Finding That Any Such Loss Was Incurred by the Cotton Company.

Assignments of Error Nos. 1, 2, 3, 15, 22, 27, 28 and 29.

The Facts.

The gist of plaintiff's first cause of action as pleaded and of the findings of fact as made by the trial court, and of the opinion of the learned trial judge is *that by the acts of fraud and misrepresentation J. B. Sears in his official capacity as secretary of the Cotton Company, obtained delivery to the Cotton Company from the plaintiff bank of 1091 warehouse receipts evidencing 1091 bales of cotton; that in violation of the agreement made by the Cotton Company with the bank, and in violation of the trust receipts executed by the Cotton Company in favor of the plaintiff bank, said Sears, as secretary of the cotton company, converted and wilfully misapplied as to the plaintiff bank, the said warehouse receipts, the cotton represented thereby, and the proceeds from the sale thereof, by selling the cotton and using the proceeds from the sale thereof in the general business of the cotton company, including pay-*



*ment of its operating expenses, instead of paying over such proceeds to the bank in discharge of the trust receipts.* It is expressly pleaded [see plaintiff's complaint, page 28], and is expressly admitted [page 376] that the total proceeds from the sale of the 1091 bales of cotton were deposited in the general checking account of the Cotton Company and used in the Cotton Company's business. It is not contended that any of said cotton, or the proceeds thereof, was wrongfully converted or misapplied as to the Cotton Company itself, but that the wrongful conversion and wilful misapplication was as to the plaintiff bank. It is contended by the plaintiff bank that by reason of the wrongful conversion and wilful misapplication by the Cotton Company through the acts of its secretary, J. B. Sears, of the 1091 warehouse receipts and the cotton and proceeds from the sale of cotton represented thereby, the Cotton Company became responsible (that is, liable) to the bank for the reasonable market value of the property so wrongfully misapplied to the Cotton Company's use instead of to the bank's use as agreed upon between the Cotton Company and the bank and as expressly provided in the trust receipt.

Irrespective of whether the acts of Sears were wilful or fraudulent, there can be no question but that the Cotton Company converted and applied to its own use the 1091 warehouse receipts and the cotton and proceeds from the sale of the cotton represented thereby and that by reason of such conversion it, the Cotton Company, became liable to the plaintiff bank in a sum equal to the reasonable value of the property. The

fact that such liability exists, however, does not for a single moment warrant the conclusion that the Cotton Company itself sustained any loss by reason of such liability having been incurred through the wrongful acts of its secretary. A liability equal, if not greater, already existed in favor of the plaintiff bank against the Cotton Company by reason of the fact that the plaintiff bank had advanced and paid for the Cotton Company's account the full purchase price of the 1091 bales of cotton. The day the purchase price drafts were paid that liability existed. Later the collateral securing this liability was surrendered to the Cotton Company and trust receipts given under which the Cotton Company agreed to return the collateral or the proceeds from the sale thereof. Instead of returning the property or the proceeds it sold the property and used the proceeds in its own business. By reason of this use, the Cotton Company became liable to the plaintiff bank for the value of the property so converted, but that value would be the reasonable market value of the property and for all general purposes might be considered to be identical in amount with the liability which already existed in favor of the bank by reason of its having advanced the money to the Cotton Company to purchase the cotton. As found by the trial court [finding No. XI, page 140], the plaintiff bank took judgment against the Cotton Company for the full amount of this liability—to-wit, the amount which the bank advanced for the Cotton Company in the purchase of the 1091 bales of cotton. It is true that the liability for moneys advanced by the

bank is a contractual liability, while the liability for the conversion of the warehouse receipts is a liability for damages. In either case, however, the Cotton Company received an amount equal to the measure of liability—that is, in the first case, it received the full benefit of the money advanced by the plaintiff bank on account of the purchase price of the cotton, and in the second case it received (converted to its own use) property of a value equal to its liability for the conversion thereof.

Without seeming to restate a self-evident proposition at too great length, it is respectfully submitted that the case is the same as if “A,” an attorney, had in his employ one “B” as secretary, and “B,” while acting within the scope of his duties as secretary, should wrongfully convert or misapply certain securities which had been entrusted to “A” by “C,” one of his clients, and where “B” turned over to “A,” his employer, the full value of the securities of “C” so wrongfully converted. In that case “A” could not recover on a fidelity bond covering “B” and which provided, as does the bond in question in this case that the bonding company would reimburse the insured for any loss of “money, securities or other personal property (including that for which the employer may be responsible to others).” In this case “A” would be responsible (liable) to “C” for the property so wrongfully converted by the employee “B,” but “A” could not recover on the fidelity bond covering “B” for two reasons: First, because “A” suffered no loss by reason of having incurred the responsibility (liability) to “C,” since he received prop-



erty belonging to "C" of a value equal to the liability; and second, because "A" could not be permitted to recover for any loss resulting from wrongful acts, he having received the full benefit of such wrongful acts.

The interpretations placed upon the bond by learned counsel for defendant in error and apparently by the trial court in its opinion is that the bond is broad enough to make the bonding company a guarantor of all liabilities contracted by the Cotton Company through the fraudulent practice of its secretary, J. B. Sears.

It is important to note carefully the terms of the bond which provide that the bonding company

"shall reimburse the employer for any loss \* \* \* which the employer shall have sustained by reason of any acts, etc."

Counsel for plaintiff bank interpret this language as synonymous with,

"the bonding company will reimburse the employer for any liability which the employer shall have incurred by reason of any act or acts of fraud, etc."

Such a construction is wholly unwarranted. The word "loss" and "sustain" have well defined meanings and are not ambiguous. They are not synonymous with "liability" and "incur." To illustrate, if Sears with a fraudulent intent and desire to cause a loss to the Cotton Company and the bank had by false and fraudulent representations and while acting within the scope of his duties as secretary, borrowed from the plaintiff bank \$100,000.00 and had diverted the



money to his own use or to the use of some party other than the Cotton Company, a *loss* would have been *sustained* by virtue of the fraudulent acts, and likewise a *liability* in favor of the bank would have been incurred against the Cotton Company in favor of the bank in the sum of \$100,000.00. If, however, as in the case at bar, the \$100,000.00 so acquired by Sears from the bank in the name of the Cotton Company was paid into the treasury of the Cotton Company and it received the full benefit thereof, the Cotton Company would *sustain* no *loss* but the liability of the Cotton Company to the bank would have been *incurred* and could be enforced.

*It must be kept in mind that the bond in the present case is not in favor of the plaintiff bank and no liability on the bond can be predicated upon any loss of the bank, whether the loss arose out of the fraudulent acts of Sears or otherwise.*

It was urged by learned counsel for defendant in error at the trial in the lower court that by reason of concealment of the facts regarding the true financial condition of the Cotton Company the other officers permitted the Cotton Company to continue its operations on a declining cotton market, and that such continuation of the business resulted in the Cotton Company losing all the proceeds which it realized from the sale of the 1091 bales of cotton which it received from the bank. The business of the Cotton Company was conducted in the same manner during the second year as it was during the first year. The financial results were different not by reason of the fact that Sears

handled the business of the Cotton Company in its dealings with the bank any different during the second year than during the first, but because during the first year the cotton market was rising, and during the second year it gradually declined from 40¢ to as low as 8¢ per pound, reaching the low point about the time of Sears' death.

Defendant in error urged to the trial court that Sears committed a fraud upon the Cotton Company in misrepresenting or concealing the fact during the second year that the Cotton Company was losing money and in misrepresenting the fact as to the cotton being hedged. Conceding for the sake of argument that such misrepresentations were made, such fact would not be a basis upon which a loss, for which the bonding company is liable, could be predicated. The entire management of the Cotton Company from its inception was in the hands of Sears, his power as secretary and general manager being unlimited; all questions regarding the operation of the Cotton Company were left to Sears. It is quite apparent that the other officers were satisfied with his management and conduct during the first year, notwithstanding the fact that he did business for the Cotton Company with the plaintiff bank the same way during the first year that he did during the second. If the cotton market had been a rising one during the second year and a net profit had been made instead of an operating loss, no criticism would have been made of Sears' conduct.

It is pleaded by plaintiff [page 50] and urged by plaintiff to the trial court that assets of the Cotton

Company, and particularly the proceeds from the sale of the 1091 bales of cotton which belonged to the bank, were lost to the Cotton Company by its speculation on the cotton market. The facts are the Cotton Company was at all times speculating—that is, buying at the market, and selling at the market. The very nature of its business was speculative. At no place in the record is it suggested that J. B. Sears was not a skilled broker, or that he did not at all times use good judgment in the purchase and sale of cotton. Admittedly, the 1091 bales of cotton in question were sold for the fair market price and the Cotton Company received the proceeds thereof. Thereafter, more cotton was bought and by reason of the declining market a deficit was incurred and the Cotton Company was unable to meet its obligation to the bank.

It was further urged that Sears committed a fraud on the Cotton Company by misrepresentations to the other officers that the cotton was being hedged. The question of whether cotton should or should not be hedged was left entirely to Sears, and the question of hedging is one on which brokers do not agree. "Hedging" is selling and buying cotton on the market at the same time the sales protecting the purchases, and vice versa. It limits the profit to a commission and often results in a loss equal to the commissions. The testimony of Mr. Norsworthy is that Sears received positive instructions from Mr. Neal of the McFadden Company, under whose guiding hand the brokerage business was being conducted, not to hedge,



and Norsworthy further testified that he had been in the cotton brokerage business for many years, and that it was not, in his opinion, good practice to hedge.

It was further urged by defendant in error that Sears committed a fraud upon the Cotton Company by not advising the other officers that the proceeds from the sale of cotton covered by trust receipts were being used for payment of general operating expenses. The exclusive management of the Cotton Company was entrusted by the other officers to Sears and that Sears did the best he could in view of the falling market and lived in the hope of a turn in market conditions, is not disputed. It was the vicissitudes of the cotton market that brought about the disastrous result.

All the foregoing complaints regarding the good faith of Sears toward the Cotton Company, however, are not material in view of the fact that the loss which the plaintiff bank seeks to recover is the loss (liability) of the Cotton Company to the plaintiff bank by reason of the conversion to the Cotton Company's use of the 1091 bales of cotton, for which the bank held trust receipts. *The loss sought to be recovered herein is not predicated upon any operating loss incurred by the Cotton Company during the time that Sears was managing the company.* If so, then what portion of that loss was incurred before December 1st, 1920, when Sears became the owner of the corporation, and what portion was incurred thereafter? This question cannot be answered from the record. As stated, such operating loss of the Cotton Company, however, is



not the basis of loss sued for in plaintiff's first cause of action.

A considerable portion of the record is devoted to proof of Sears' concealment of facts from the other officers of the Cotton Company and of his breach of the trust receipts and agreements made by the Cotton Company with the plaintiff bank. There is no evidence of any kind or character that Sears ever prior to a short time before his death, spoke a single word to any officer of the plaintiff bank concerning the securing delivery of the cotton tickets and the substitution of trust receipts, or concerning the sale of the cotton and the disposing of the proceeds in the checking account, other than that Sears made the initial arrangement for handling the finances of the Cotton Company at the bank as set forth in the letter of September 8, 1919.

Mr. Ivy, in charge of the note department of plaintiff bank, one of the principal witnesses for the plaintiff, does not testify to any conversations had with Sears in relation to the transaction between the Cotton Company and the bank, except those that occurred shortly prior to Sears' death, and long after the alleged loss was incurred. Likewise, Mr. Pettigrew and Mr. Rugg, vice presidents of the plaintiff bank, each testified that no representations were made to them by Sears concerning the handling of the securities, etc. They were the only officers of the plaintiff bank whose testimony was introduced.

Mr. Norsworthy testified [page 457] that he was the one who took the first "outbound documents" to

the plaintiff bank and secured the "OK" of a vice president and deposited it as a cash item, and that it was he who usually attended to the drawing of checks and the payment of acceptances and securing return of trust receipts. He testified [page 403] that he did this, not under instructions from Sears, but because it was the usual and customary way of handling the business, being the method which was employed by many large brokerage concerns with whom he had been employed. Likewise, Mr. West testified [page 341] that the manner in which the Cotton Company handled its business with the bank during its two years of operations was in accordance with the usual manner of dealing between banks and cotton brokerage concerns and met with his approval. Mr. McDevitt testified [page 273] as well as did Mr. West [page 340] that the plan of operations between the Cotton Company and the bank, as outlined in the letter of September 8, 1919, was known to them and met with their approval; that they knew and approved of the delivery by the bank to the Cotton Company of the warehouse receipts and the substitution of trust receipts therefor. that they knew and approved of the sale of the cotton and the depositing of the proceeds of sale by the cotton company in its general checking account [page 343]; and that the only thing in the whole plan of operation between the cotton company and the bank that they did not know and would have disapproved of was that any portion of the proceeds from the sale of cotton for which the plaintiff bank held trust receipts should be used for

purposes other than payment to the plaintiff bank in discharge of the trust receipts, and that they [page 344] would not have approved had they known that the general operating expenses of the cotton company were being paid out of the proceeds of cotton covered by the trust receipts held by the bank.

Having in mind that the same plan of handling the finances of the cotton company and the payment of trust receipts obtained throughout the two years during which more than a million dollars of cotton was bought through and paid for to the plaintiff bank, all of which was clearly reflected in the books of the cotton company, it is hard to conceive how either the plaintiff bank or the other officers of the cotton company can be heard to say that they had no knowledge that the cotton company was handling the proceeds of cotton covered by trust receipts in the manner in which it did. Mr. Ivy, one of the vice presidents of plaintiff bank, when confronted with the fact that during the first year 92 acceptances with trust receipts attached, and during the second year 77 acceptances with trust receipts attached, were paid to the bank by the cotton company by checks drawn on the general checking account, and that in no single instance was the trust receipt literally complied with (that is, the "outbound document" returned to the bank in discharge of the trust receipt) frankly admitted that the bank was not concerned [page 376] as to how the acceptances were paid and the trust receipts discharged.

In view of the foregoing it is difficult to understand how any finding could be made that both the bank



and the other officers of the cotton company did not know and did not approve of the manner in which Sears was handling the cotton company's business. Furthermore, the officers of the cotton company were duty bound as officers and directors to know, and if they saw fit, to take no part whatsoever in the operation of the cotton company's affairs (and each testified that he took no active part), then they should not be permitted to complain that as a result of the operations the cotton company incurred liabilities for which it had no assets to cover. Furthermore, it must be reiterated that the fraud and deception which it is alleged Sears practised upon the cotton company by misrepresentation or concealment of facts or by failure to keep proper entries within its books, is not the basis upon which the loss sought to be recovered herein is predicated. The loss sued for herein is that resulting from liability incurred in favor of the plaintiff bank by the Cotton Company through the alleged wrongful conversion of the Cotton Company of 1091 bales of cotton in which the bank had an interest. While this liability was incurred, the Cotton Company sustained no loss by reason thereof, because it received the full benefits of the conversion of the property upon which the liability to the bank is predicated.



II.

The First Cause of Action in Plaintiff's Complaint as Amended Does Not State Facts Sufficient to Constitute a Cause of Action Against Defendant Bonding Company and the Trial Court Erred in Overruling Defendant's Demurrer Thereto and in Refusing to Find Judgment for the Defendants.

Assignments of Error Nos. 1 and 2.

The foregoing point is predicated upon the contention of plaintiff in error that plaintiff's first cause of action as pleaded shows affirmatively that the cotton company received and converted to its own use and benefit all of the property—to-wit, the 1091 bales of cotton, the liability for which by the Cotton Company to the bank, is the basis of the alleged loss upon which plaintiff seeks recovery. This matter has been argued at considerable length under a previous point in this brief and it is unnecessary to reiterate such statement. The trial court finds that the bank did sustain a loss by reason of the wrongful conversion of said 1091 bales of cotton. The conversion was made, by the arguments of the complaint, by the cotton company by its secretary while acting within the scope of his duties. The reasonable value of the cotton so converted was received by the Cotton Company and used for its own purposes. This is affirmatively pleaded in plaintiff's complaint [pages 46 and 49]. That the Cotton Company incurred a liability for the value of the property so converted to its own use, does not

amount to a "loss" under a fidelity bond against "loss." Mere liability is not sufficient.

It must be kept in mind that the theory of plaintiff's complaint and the whole basis of the learned trial judge's opinion is based upon the finding that the Cotton Company by and through the wrongful acts of its secretary, J. B. Sears, while acting for the Cotton Company and in the scope of his duties, wrongfully secured from the plaintiff bank 1091 warehouse receipts covering 1091 bales of cotton and wrongfully sold the cotton and converted the proceeds to the use of the Cotton Company's business. Neither the complaint nor the opinion of the trial judge predicates any loss to the Cotton Company by reason of the operating loss which was sustained by the Cotton Company during the second year of its operations, and no evidence was introduced to show the extent of any such operating loss. The trial court holds that the word "loss" in the bond sued upon is equivalent to the word "liability" where such liability arose out of the wrongful conversion by the Cotton Company through its secretary, of property in which the plaintiff bank had an interest—to-wit, the 1091 cotton tickets for which the plaintiff bank held trust receipts; and this notwithstanding the fact that it is admitted by all parties concerned that not one dollar of the proceeds from the collateral so converted was used by J. B. Sears personally or by any person, firm or corporation other than the Cotton Company itself.

To concede any such conclusion as contended for by the plaintiff bank is in effect to make the surety on

a fidelity bond a guarantor of every dollar of indebtedness fraudulently contracted by the risk, irrespective of whether the principal received the full benefit of the property so fraudulently obtained. Plaintiff in error respectfully submits that there is no ambiguity or uncertainty in the bond which would justify any such forced construction, and nowhere in the adjudicated cases or in text books has counsel for plaintiff in error been able to find any authority that makes or suggests any such possible construction, notwithstanding the fact that there are literally thousands of adjudicated cases involving bonds similar to the bond in question.

## THE LAW.

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**The Bond Sued Upon Is Strictly One of Indemnity,  
That Is, One Against Loss and Not One  
Against Liability.**

As found by the trial court [finding No. XI, page 140], judgment was obtained by the plaintiff bank against the Cotton Company covering the liability of the Cotton Company to the bank on account of acceptances and trust receipts. It is admitted that this liability has not been paid by the Cotton Company to the bank.

**An Indemnatee Cannot Recover on an Indemnity Bond by Mere Liability Until Such Liability Has Been Paid.**

See 31 C. J., page 439, and long list of cases cited therein.

The courts of California have interpreted the provisions of a bond against "loss which he may ever sustain" in a number of cases and have held that mere liability for loss is not sufficient. See

Fernandex v. Tormor, 121 Cal. 515;

Oakes v. Scheifferly, 74 Cal. 478.

**To Constitute a Loss the Misapplication Must Be to the Use of Some Person Other Than the Insured.**

In *United States v. Butte*, 107 U. S. 655, the court held that to constitute the offense of "misapplication," "there must be a conversion to his own use or to the use of someone else of the moneys and funds of the association by the party charged."

In *United States v. Breese*, 173 Fed. 402, at page 406, the court said:

"Wilful misapplication as described in the statute means a misapplication wilfully and unlawfully made by one or more of its officers of the moneys, funds or credits of the bank, and done with intent to injure the bank, and the funds so misapplied must be converted to the use of the officer or officers making such application, or to the use of some other person than the bank."



Frost on Guaranty Insurance, 2nd Edition, Sec. 477, defines "misapplication" and misappropriation" as being,

"the wilful and wrongful use of money, property or effects entrusted to the party charged for some particular purpose and by him converted to the use of himself or to the use of others than the lawful owner."

In *Rosentee v. American Surety Co.*, 91 N. J. L. 591, the court says:

"The funds of a trust company are wrongfully misapplied by its teller when he converts it to his own use or benefit or to the use or benefit of someone other than the trust company with intent to injure and defraud the trust company."

**The Bonding Company, as Insurer, Cannot Be Held Liable Under the Bond for Any Mere Errors of Judgment or Injudicious Exercise of Discretion on the Part of Sears, the Risk, in and About All of the Many Matters Wherein He Was Vested With Discretion, Either by Instructions or by Rules and Regulations of the Insured.**

In the case of *Monongehela Coal Co. v. F. & D. Co.*, 94 Fed. 732 (C. C. A. 5th Circuit) on the settlement of accounts the agent owed the employer; held, it was not proven that the employer "diverted from employer moneys"; and that the loss resulting from the carelessness or inattention to business might be the foundation of a just claim against the employee but it would impose no liability upon the bond.

In the case of *Clark v. F. & D. Co.*, 73 Wash. 65, suit was brought upon a fidelity bond covering sales from consigned goods to one Miss Churchill. She re-located her business and lost money and was short in her remittances covering merchandise she had sold from consigned stock.

“She appropriated the money to what she deemed to be the demands of the business for the mutual benefit of herself and consignor. She did not misappropriate it to her own use or make such a conversion of it as to subject her to a charge of larceny.”

The court held that the bond protects the consignor against dishonesty of Miss Churchill and not against her lack of business knowledge.

The court at all times in considering this case must keep in mind that it is expressly pleaded that the proceeds from all of the property which it is held was, as to the bank, wrongfully converted, was deposited to the credit of the Cotton Company and used in its business.

### Scope and Construction of Bond.

In construing contracts of insurance, the court must be guided by the rule suggested by the United States Supreme Court in the leading case of *Guaranty Company of N. A. v. Mechanics Savings & Trust Co.*, 183 U. S., 407, where, speaking of strict interpretation of bonds, the court said:

“But this rule cannot be availed of to refine away terms of a contract expressed with sufficient clearness to convey the principal meaning of the parties, and embodying requirements, compliance with which is made the condition of liability thereon.”

As clearly pointed out by the cases cited in this brief, under the heading “Failure to comply with promissory warranty,” a failure on the part of the insured to make at least a substantial compliance with the requirements of the bond does relieve the surety company, and the courts will not, under the doctrine of strict compliance, refine away the terms made in the contract of insurance.

It is the contention of defendant in error and seems to be the view adopted by the trial court that the parenthetical clause contained in the bond—to-wit, “including that for which the employer may be responsible to others” is explanatory of the word “loss;” and further that the word “loss” is synonymous with the word “liability.” They conclude therefrom that the bond is in effect an agreement to reimburse the Cotton Company for any liability to the plaintiff bank arising out of the wrongful conversion by the Cotton Company to its own use of property in which the bank had a property interest.

Plaintiff in error urges that the parenthetical clause above referred to, being the usual and ordinary provision in fidelity bonds, is explanatory of the words “money, securities or other personal property,” and not of the word “loss.” It is designed to cover loss

sustained by the insured through the wrongful conversion by the risk of property of others held by the insured as bailee.

*City Trust etc. Co. v. Lee*, 204 Ill. 72.

In this case the provision of the bond was that it should cover "dishonesty or any act of fraud (amounting to larceny or embezzlement)". In interpreting this clause the court laid down the following rule of interpretation:

"In the construction of written instruments a qualifying phrase is to be confined to the last antecedent unless there is something in the instrument which requires a different construction. This rule has been enforced in many cases."

Applying the above principle to the case at bar, it is apparent that the qualifying phrase "that for which the employer may be responsible to others" is by the rule of syntax explanatory of the words "property, etc.," and not the word "loss."

Fidelity guaranty insurance is a contract of indemnity and not one insuring against liability.

Joyce on Insurance, 2nd Ed., section 2766.



III.

There Is No Evidence to Support or Justify the Findings of the Trial Court as Set Forth in Findings No. VII That the Reasonable Value of the 1091 Bales of Cotton Sold and Disposed of by the Cotton Company and for Which the Plaintiff Bank Held Trust Receipts, Was at the Time the Same Were Sold and Disposed of, of the Reasonable Value of \$60,594.62; or to Support Finding No. XXIV That the 455 Bales of Cotton Covered by Warehouse Receipts Delivered by Plaintiff Bank to the Cotton Company Prior to December 1st, 1920, and Not Returned to the Bank, Were at the Time They Were Sold of the Reasonable Value of \$29,336.99.

Assignments of Error Nos. 11 & 26.

The loss for which the bonding company is held liable by the decision of the trial court is the amount in which the Cotton Company became liable to the plaintiff bank for having failed to return a certain number of warehouse receipts or the proceeds from the sale of the cotton represented thereby, as expressly provided in the trust receipts. Had the total proceeds from the sale of the cotton covered by trust receipts been returned to the plaintiff bank, the trust receipts would have been fully satisfied and discharged. It is respectfully submitted, therefore, that the amount of loss (liability) of the Cotton Company to the bank must be measured by the amount realized by the Cotton Company from the sale of the particular cotton, or in any event, the reasonable market value of such cotton at the time it was sold and disposed of. The undisputed evidence shows that every bale of

the cotton in question was sold by the Cotton Company at a price considerably less than the original purchase price, by reason of the steady decline in the cotton market. The record shows [page 436] that during the second year, on the average, every bale sold for \$12.00 less than the cost. The Cotton Company was bound by the trust receipts to return either the warehouse receipts or the proceeds from the sale of the cotton, and if an amount less than the original purchase price was received when the cotton was sold, the trust receipts would have been fully discharged by a return of such sale price. There is no contention that any of the cotton in question was not sold at the then reasonable market value.

The trial court, however, fixes the loss (liability of the Cotton Company to the bank for unreturned warehouse receipts) in an amount equal to the original cost price of the cotton to the Cotton Company. It is conceded that the Cotton Company owed the plaintiff bank an amount equal to the original cost price of the cotton, because the bank had paid the purchase price drafts for the Cotton Company, that is, advanced the money to pay for the cotton, but such liability for moneys so borrowed from the bank is not the liability upon which the plaintiff in its complaint, or the trial court in its opinion, fixes the loss. The trial court expressly holds in its opinion [page 180] that the loss for which the bonding company is liable is an amount equal to the liability of the Cotton Company to the bank for the misapplication of the proceeds from the sale of the cotton in question by the Cotton Company. The measure of damage for failure to return the "out-bound documents" as expressly provided in the trust receipts, must be measured by the sale price of the cotton and not by the original purchase price.

IV.

The Cotton Company During the Latter Part of 1920 Became a Corporation Sole—To-wit, J. B. Sears, and Thereafter J. B. Sears, the “Risk” Named in the Bond, Was in Complete Ownership and Control of the Cotton Company. That on and After the Date When Such Complete Ownership and Control Was Obtained by J. B. Sears the Cotton Company—To-wit, J. B. Sears, Had No Right of Action to Recover for Any Loss Sustained by the Wrongful Acts of J. B. Sears, Whether Committed Prior to or Subsequent to the Date on Which the Ownership and Control of the Cotton Company Was Acquired by Sears. For That Reason the Trial Court Erred in Finding Judgment Against Defendant and in Refusing to Grant Defendant’s Motion for Judgment for Defendant. In View of the Finding of Fact That the Cotton Company Became a Corporation Sole—To-wit, J. B. Sears, on December 1st, 1920, the Trial Court Erred in Its Conclusions of Law That the Plaintiff (Assignee for Collection of the Cotton Company) Was Entitled to Judgment for Any Loss Resulting From the Wrongful Acts of J. B. Sears.

Assignments of Error Nos. 2, 25, 27, 28, 30.

Facts.

The trial court in its findings of fact [finding No. 21, pages 148-151], finds that prior to December 1st,



1920, the Cotton Company was merely a medium through which T. J. West was conducting his cotton brokerage business and was in fact a corporation sole—to-wit, T. J. West. During this period of time Sears was merely an employee and that relationship necessary in all cases of fidelity insurance, to-wit, “principal” and “risk” existed. The court further finds that on December 1st, 1920, the complete ownership and control of the Cotton Company passed from the principal, T. J. West, to the risk, J. B. Sears, and that after December 1st, 1920, the Cotton Company was a corporation sole—to-wit, J. B. Sears. This situation continued and at the time of the death of J. B. Sears on May 3, 1921, he was still the owner of the Cotton Company and so far as the record shows, the ownership of the Cotton Company passed to and remains an asset of his estate. Thereafter—to-wit, on the first day of September, 1921, the Cotton Company assigned for collection to the plaintiff bank its cause of action, if any, existing against the bonding company on the bond.

As clearly expressed by the learned trial judge in his opinion [page 174], “This action must be considered having in view only the obligations created by the bonding company toward the cotton company, and strictly as though there had been no assignment.” This for the reason that the plaintiff bank is a mere assignee for collection and as such assignee could have no greater rights than the cotton company—to-wit, J. B. Sears, a corporation sole. Therefore, in the argument upon this point we will disregard the assignment



and consider solely the question whether or not the cotton company had any right of action against the bonding company at the time this action was filed for any loss that may have been sustained by reason of any wrongful acts of J. B. Sears.

After Sears' death the cotton company filed its proof of loss with the bonding company for an alleged loss aggregating in excess of \$60,000.00 resulting from alleged wrongful acts done by J. B. Sears while acting as secretary of the cotton company. If such a valid claim against the bonding company for recovery of the loss existed under the bond, such claim constituted an asset of the cotton company and existed prior to Sears' death as well as subsequent to his death, although it could not ripen into a cause of action until a proof of claim had been duly filed with the bonding company. The fact that Sears died does not affect the situation as to the right of the cotton company to recover. It was merely an unfortunate incident in the matter. The corporation for all legal purposes was just as much a corporation sole—to-wit, the estate of J. B. Sears, after his death as it was a corporation sole immediately prior to his death. Admittedly during Sears' life time the cotton company—to-wit, J. B. Sears, could not have maintained any action at law to recover from the bonding company any loss resulting from any fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears of the cotton company's property, or of any property in which the cotton company was interested for the very self-evident reason that

to permit such recovery would be to permit J. B. Sears to benefit directly from his own wrong. Any sum recovered after December 1st, 1920, by the cotton company from the bonding company by reason of loss resulting from the wrongful acts of J. B. Sears would have been solely for the benefit and use of J. B. Sears or of his estate, he being the corporation sole.

The trial court very properly held that any loss resulting from the wrongful acts of J. B. Sears after he became the corporation sole could not be recovered from the bonding company because from that date on the very fundamental relationship of "principal" and "risk" was destroyed—that is, the relationship of employer and employee ceased to exist; and for the further fundamental reason that Sears, doing business through the cotton company, could not recover any loss resulting from his own wrongful acts. It is respectfully submitted that the trial court erred in its conclusions of law from the fact found that the cotton company became and was a corporation sole—to-wit, J. B. Sears, on and after December 1st, 1920, that the cotton company (that is, J. B. Sears), could thereafter recover for any loss that may have been sustained by the cotton company prior to December 1st, 1920, by reason of the wrongful acts of J. B. Sears. The rule that a man cannot recover damages resulting from his own wrongful acts would work effectively against recovery by the cotton company (that is, J. B. Sears), whether such loss was incurred by reason of wrongful acts of J. B. Sears performed prior to December 1st, 1920, or subsequent thereto.

It is respectfully submitted that when J. B. Sears purchased all of the stock of the cotton company from West he acquired thereby the ownership of any claim which West or the said cotton company had against the bonding company arising from the wrongful acts of J. B. Sears, and that the acquisition of ownership by Sears of such claim based upon his own wrongful acts, terminated all liability on such claim, and that Sears, doing business as the cotton company, could not have enforced any such claim against the bonding company. Such claim, if any existed in favor of the cotton company, a corporation sole—to-wit, T. J. West, ceased to exist when the cotton company became a corporation sole—to-wit, J. B. Sears, and said claim was terminated and extinguished and thereafter there was no claim in existence which could have been assigned to the plaintiff bank herein. No person has any enforceable claim for loss resulting from his own wrongful acts and, therefore, such person cannot by assignment give any rights to an assignee.

## THE LAW.

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The Liability of an Insurer Is Never Greater Than the Liability of the Risk to the Insured. The Merging of the Risk (J. B. Sears) and the Insured (Cotton Company) in the Same Person Extinguished the Claim and Released the Liability of the Insurer.

The Sale by West, a Corporation, to Sears, a Corporation Sole (the Risk), Released Sears as Principal on the Bond—Which Release Discharged the Surety.

“The policy of fidelity insurance being essentially one of indemnity, to enforce a claim thereunder against the insurer for the benefit of an insured, who had no concurrent existing legal claim against the ‘risk’ therefor, would be to change the nature of the agreement from one of indemnity to that of a wagering contract. To entitle the insured to recover under a fidelity insurance policy, it is in every instance incumbent upon him to show some invasion of his legal rights on the part of the ‘risk’ which in itself constituted, at the time such recovery is sought, a valid enforceable claim against the ‘risk’ in favor of the insured.” Frost on Guaranty Insurance, Second Edition, page 69.

Independent School District v. Hubbard, 110  
Ia. 58; 81 N. W. 241;

Volume I, Cooley’s Briefs on Insurance, pp.  
236-237.

The Supreme Court of North Carolina in a recent case, *Blades v. Dewey*, 48 S. E. 26, stated the general



principle governing contracts of compensated suretyship as follows

“Every contract of suretyship is based upon some contract made or obligation assumed by the principal obligor, and the liability is measured by the obligation of the principal.”

Electric Appliance Co. v. U. S. Fid. & Guar. Co., 110 Wis. 343; 85 N. W. 648;

Am. Sur. Co. v. U. S., 28 Sou. Rep. 664;

Iowa Tillooet Gold Mining Co. v. Bliss, 144 Fed. 446.

Frost in his treatise on Guaranty Insurance (page 352) says:

“In general there can be no recovery had by the insured against the insurer under a policy unless there is in existence at the same time a valid and enforceable claim against the ‘risk’ for the same cause in favor of the insured. The reason of this is obvious. Fidelity insurance is a contract of indemnity only, and further it is an indemnity against loss arising from acts of the ‘risk’ in breach of his own contract obligations to the insured. Thus an unquestioned limitation on the insurer’s liability is that the claim shall be a valid and enforceable one against the ‘risk’ in favor of the insured. Were this not so, the valued right of subrogation would be worthless to the insurer, as he could not in any event recover of the ‘risk’ the amount he had paid to the insured on an invalid and unenforceable claim.” \* \* \*

[Page 353]: “As it is a sound principle of law that the obligation of the insurer to the insured can never be greater than the liability of the ‘risk’

to the insured, so it may be said that the law implies from policies of guaranty insurance the condition, irrespective of express conditions in the policy to that effect, that the liability of the 'risk' to the insured after a loss has occurred, for which the insurer is liable to the insured under the policy, shall not be changed in any material respect. This on the principle that the inchoate right of subrogation belonging to the insurer under such circumstances is a valuable right, and that for this reason no material change in the status of the 'risk' with respect to the latter's liability to the insured, as it existed at the time the loss occurred, will be permitted."

Again on page 402 the learned author says further:

"Discharge of Insurer's Liability by Formal Release of the 'Risk's' Liability Running From the Insured to Such 'Risk.' Fidelity insurance is pre-eminently a contract of indemnity. Therefore there can be no legal liability incurred by the insurer under a policy of fidelity insurance, unless there exists at the same time a liability at least as coextensive on the part of the 'risk' to the insured. Furthermore it follows that when there is a voluntary release on the part of the insured of the 'risk's' liability to it, such release has the effect in law of releasing the insurer from liability—if such exists—to the insured on account of the matter covered by the release of the 'risk' by the insured. A similar result is arrived at whenever the liability of the 'risk' to the insured is satisfied by payment of the debt represented by such liability. In other words the principal obligation—that of the 'risk' to the insured—being satisfied, the incidental obligation—that of the

insurer to the insured—is likewise discharged.” See *Perpetual Bldg. & Loan Assn. v. U. S. Fid. & Guar. Co.*, 118 Ia. 729; 92 N. W. 686.

“It is doubtless true that even where the insured secretly receives from the ‘risk’ the full amount of the insurer’s liability on account of a loss covered by the policy, he will be held in law, under a well-recognized rule of subrogation, to hold such payment in trust for the insurer, as the law will not permit him to profit by a recovery for the same debt against both the insurer and the ‘risk’. See *Am. Sur. Co. v. Lawrenceville Cem. Co.*, 110 Fed. 717; *C., St. L. & N. O. Ry. Co. v. Pullman, Sou. Car. Co.*, 139 U. S. 79.”

It is respectfully submitted that under the general principles of law in relation to suretyship above announced no liability on the part of the bonding company exists, because no valid and enforceable claim existed in favor of the cotton company, a corporation sole—to-wit, J. B. Sears (the insured) against J. B. Sears (the risk) after December 1st, 1920, and at the time of the attempted assignment by the cotton company to the plaintiff bank no claim in fact existed.

The finding of the trial court that the cotton company became a corporation sole—to-wit, J. B. Sears, was proper. In a recent case decided by the Supreme Court of California, *Wenban Estate v. Hulette*, 67 Cal. Dec. 493; 227 Pac. 723, the court held that where a corporation is but the instrumentality through which an individual transacts his business, the corporation will be bound by the acts of the sole stockholder just as it would be bound if the corporation did not exist.



This decision is in keeping with prior California decisions and also in line with decisions of this court. See *Miller and Lux v. Ricker*, 146 Fed. 574, affirmed by the United States Supreme Court in 218 U. S. 258. In that case the court held that where suit is brought by a riparian owner to enjoin another riparian owner from diverting the water, and the latter, pending the suit, converts his rights to a corporation organized for that purpose and owns all its stock, such corporation is bound, although not a party to the suit, for the reason that the corporation was merely the person under another name.

See also case, *Mills v. The Richmond Co.*, 63 Cal. App. 594, in which the court held that when an individual conducts his business under a corporate name owning all of the stock of the corporation, except a few qualifying shares, the difference between the individual and corporate entities will be disregarded if necessary to work out equitable ends.

The defendant bonding company (insurer) insured the cotton company (insured) against loss that might result from wrongful acts of its agents, Sears (the risk). All contracts of guaranty insurance imply some contractual relationship or obligation between the insured and the risk. As stated by Frost in his "Treatise on Guaranty Insurance" (Second Edition, p. 45):

"A fact that may be stated as a general principle governing all branches of guaranty insurance is that every contract of compensated suretyship is based upon some contract made or obligation assumed by the 'risk' and the liability of



the compensated surety thereunder is measured in all cases by the obligation of the 'risk' to the party for whose benefit such contract of compensated suretyship was entered into. The obligation of the insurer to the insured can never be greater than the liability of the 'risk' to the insured."

*Likewise, it is fundamental that the insured in all cases must possess what is termed an insurable interest in the policy.*

As stated again by Frost, the reason for the above rule is as follows:

"The underlying reasons which render it necessary that the insured shall have an insurable interest in all fidelity insurance policies, where liability thereunder is sought to be enforced for his benefit, are mainly three in number.

First. It is contrary to the spirit of the law, which always favors legitimate business, that it should sanction speculation on the honesty or faithfulness of one's fellow-men.

Secondly. It is opposed to the public policy in that it would permit a party to enter into a contract wherein it would be to his pecuniary interest to induce dishonesty or unfaithfulness on the part of the 'risk,' which would operate to his advantage and to another's pecuniary disadvantage. In other words, under such circumstances, dishonesty and unfaithfulness would be at a premium, and honesty and faithfulness in public or private duty the last thing sought for.

Thirdly. In view of the fact that the policy is universally executed with reference to the in-

dependent contractual or official obligations of the 'risk' to the insured, it is in harmony with the policy of the law, clearly recognized in the case of contracts identical in purpose of that entered into between the insured and the insurer in fidelity insurance, to insist that the right to enforce such contracts, as between the insured and insurer, should not be more extensive than the right to the insured to enforce the contemporaneous contractual or official obligation of the 'risk' to himself."

On this point, Mr. Cooley in his "Briefs on Insurance," page 236, says:

"The general principle emphasized in all cases, involving the extent of liability under guaranty and indemnity contracts, that the contracts are strictly contracts of indemnity, and that the measure of liability is the extent of actual loss, is strictly in accord with the principle that insurable interest is necessary, and it is consonant also with the general rule prevailing in fire and marine policies, that the extent of recovery is limited to the extent of interest. Since a guarantor cannot be held liable on his guaranty except to the extent that the original debtor or risk is liable on his contract, it is evident that under a contract of guaranty insurance the extent of insurable interest is measured by the interest in the risk."

Again Frost, on page 346, says:

"Implied Exceptions. The law implies, irrespective of express provision therefor made in the policy, certain conditions limiting the liability of the insurer to the insured under the terms

thereof. These implied exceptions to liability may be enumerated as follows:

\* \* \* \* \*

(B) From the very nature of a policy of fidelity insurance, which is at all times a contract of indemnity, it follows as one of the implied conditions of the policy that the insured should continue throughout the life of the policy to have an insurable interest therein. The recognition of such an implied condition is sometimes termed the 'doctrine of continuity of interest'."

\* \* \* \* \*

(D) One of the implied conditions of all policies of fidelity insurance is that the 'risk' shall continue to occupy the position in the employ of the insured designated in the proposal or application for the policy. Unless the policy expressly provides for changes in such employment, as, for example, expressly authorizing employment in more than one position, or changes from one position to another, there can be no recovery had by the insured from the insurer on account of defaults of the 'risk' occurring while performing duties of a position materially different from that designated in such proposal or application. The reason which induces the courts to imply such a condition as the foregoing, is that fidelity insurance companies write policies for certain designated premiums, which vary in amount according to the nature and extent of the risk incurred. If, for example, the insured asks the insurer to write a policy on a person employed as a bookkeeper in a bank, the insurer might be willing to do this at a very low premium, owing to the small chance of its ever being required to



make good any losses occasioned by such person's dishonesty while occupying the position of bookkeeper for the insured. However, if it lay within the power of the insured to change the employment at will of such person, and immediately after issuing the policy he should appoint him cashier instead of bookkeeper, it would amount to little less than a fraud upon the insurer to hold the latter liable for his acts and increased responsibilities not in contemplation of both parties at the time the policy was issued.

(E) Another implied condition of fidelity insurance policies is that there shall be no change in the composition of the insured or in the personality of the 'risk' during the life of the policy. Fidelity insurance is a personal contract, and there should be no alteration permitted either as to parties insured, or as to the 'risk' without the consent of the insurer."

In the case of *Farmers and Merchants State Bank of Verdon v. United States Fidelity & Guaranty Company*, decided by the Supreme Court of South Dakota and reported in 36 L. R. A., (New Series) 1152, suit was brought upon a fidelity bond guaranteeing the insured against loss resulting from the wrongful acts of the risk who was employed as assistant cashier. The bond, however, provided that the employee could perform other duties than those belonging to the position mentioned in the bond without any notice of such change being given to the bonding company. At the time the bond was written, the employee owned only one share of stock but later, and during the continuance of the bond, he became cashier and also ac-



quired 52% of the stock. Notice of this fact was not given to the bonding company. It was urged that the change of relationship of the employee did not affect the liability of the bonding company because it did not change the employee's duties and responsibilities beyond those provided for in the bond. The court, however, held the bonding company not liable in the following words:

“But there was a change in the employee's status in this case, not considered by the court in the Georgia decision. In that case the employee presumably continued to occupy a subordinate position, subject to the control and supervision of the corporation, acting through its board of directors. When the policy in suit was issued, James H. Carroll was the owner of only five shares of the plaintiff's capital stock; its entire capital being \$10,000. On October 10, 1903, before the alleged fraudulent acts were committed, he became the owner of 51 shares previously owned by his brother, constituting a majority of the stock, with power to select a new board of directors. After that date, he was in position to absolutely control the affairs of the bank. While in one sense he continued to be an employee of the corporation, he no longer was subject to the restraining influence of efficient supervision. He was acting as a director. Theoretically, his conduct as cashier was subject to the supervision of the other directors, so long as he allowed them to remain directors and officers of the corporation; but they were holding their positions during the pleasure of the person who owned a majority of the shares of the capital stock, and, as dis-

closed by the evidence, were, in fact, giving no personal attention to the management of the bank. It may be that their negligence in this regard would not of itself relieve the defendant of liability. On that phase of the case, no opinion is expressed. The precise question under discussion is the effect of the fact that Carroll became the owner of a majority of the capital stock, practically becoming the master of the corporation, and ceasing to be one of its servants. Clearly here was a situation not contemplated by the parties when the policy was issued, and not embraced by any fair and reasonable construction of its terms. In absence of convincing evidence, it would be unreasonable to assume that the defendant would insure the conduct of any man thus situated. An undertaking insuring a person against his own dishonesty would be, to say the least, a novel and unusual contract. *Had the plaintiff been a natural person engaged in the banking business, and this employee purchased the business or a controlling interest therein, certainly no one would contend he could maintain this action for his own benefit or that of the depositors* (Italics ours.) The object of the undertaking was to insure an employer against the fraudulent acts of an employee, not to insure an employer against his own fraudulent acts. When the person whose conduct is insured ceases to be an employee, within any fair and reasonable interpretation of the term used in the policy, the insurer's liability should cease, unless he has notice of the change. So we conclude that the facts disclosed by the records on this appeal constitute a complete defense, and that the judgment and order appealed from should be reversed."

Learned counsel for plaintiff pointed out correctly to the trial court that this decision was later over-ruled by the South Dakota Supreme court in the case of *Bank of Willow Lakes v. Syverson*, 43 South Dakota 295, 178 N. W. 989. A careful reading, however, of this later South Dakota decision does not in any way repudiate the rule annunciated in the earlier case that a substantial change of relationship between the employer and employee relieves the surety company from liability, but rather construes the change of relationship as being one contemplated by the bond.

After West sold his stock to Sears, the latter was the only party financially interested in the Cotton Company and, as found by the court became the corporation sole.

“Although the doctrine that a corporation is a legal entity and person in the law distinct from the members who compose it will always be recognized and given effect, both in law and in equity, in cases which are within its reason and when there is no controlling reason against it, and although in some cases it seems to have been given effect contrary to reason, it is clear that a corporation is in fact a collection of individuals who, in the case of modern private corporations, really own its property and carry on the corporate business, through the corporation and its officers and agents, for their own profit or benefit, and that the idea of the corporation as a legal entity or person apart from its members is a mere fiction of the law introduced for convenience in conducting the business in this privileged way; *and it is*



*now well settled, as a general doctrine, that, when this fiction is urged to an intent not within its reason and purpose, it should be disregarded and the corporation considered as an aggregation of persons, both in equity and at law."*

14 Corpus Juris, 59, Sec. 20.

In re *Rieger*, 157 Fed. 609.

In that case a partnership in the commission business buying and selling merchandise, acquired 99% of the stock of a corporation. The remaining shares were held by relatives of one of the partners. The partners held about equal amounts of the stock. It was held that the corporation was merely an agent of the partnership.

On page 614, the court say:

"In *Interstate Telegraph Co. v. Baltimore & Ohio Telegraph Co.* (C. C.) 51 Fed. 49, affirmed in 54 Fed. 50, it appears that the railroad company caused the telegraph company to be incorporated, became the sole owner of its stock, selected its own officers and employes as officers of the new company, and represented such company to have authority to contract with reference to its whole railway telegraph system. It was held that the railroad company was not only the actual owner of the telegraph company, but that the latter company was a mere department, or bureau, of the railroad company, created and maintained for the railroad company's benefit as an agent to make contracts. It follows as a corollary that, had the railroad company become insolvent while the telegraph company was in existence, the property in the possession of the



telegraph company, notwithstanding its corporate entity, would, if necessary, have been treated as property of the railroad company. The Supreme court of Ohio has repeatedly ignored the fiction of legal corporate entity when used as a shield for fraudulent or other illegal acts. The rule is clearly stated in *Bank v. Trebein Co.*, 59 Ohio St. 316, 52 N. E. 834, as follows:

“ ‘In contemplation of law, a corporation is a legal entity, an ideal person, separate from the real persons who compose it. This fiction, however, is limited to the uses and purposes for which it was adopted—convenience in the transaction of business, and in suing and being sued in its corporate name, and the continuance of its rights and liabilities, unaffected by changes in its corporate members. But the fiction can not be abused. A corporation *cannot* be formed for the purpose of accomplishing a fraud or other illegal act *under the disguise of the fiction*; and, *when this is made to appear, the fiction will be disregarded by the courts, and the acts of the real parties dealt with as though no such corporation has been formed*, on the ground that fraud vitiates everything into which it enters, including the most solemn acts of men. \* \* \* The good faith of the parties to such a transaction must be determined by its legal effect on the rights of others. If its legal effect works a fraud on their rights, the finding of the court that the parties acted in good faith is simply an erroneous conclusion of law from the facts’.”

(Citing many cases.)

Meily Co. v. London & Lacashire Fire Ins. Co., 148 Fed. 683. (Circuit Court of Appeals, Third Circuit.)

The syllabus is:

“Evidence which warrants a finding that the property of a corporation plaintiff was wilfully burned by its president, who had full control of its affairs and was the owner of practically all of its stock, the remainder being owned by members of his family; that the business was on the decline, the lease about to expire, and the property over-insured; and that the over-valuation was participated in by other members of the family—is sufficient to charge the corporation with the act of incendiarism, and to constitute a defense to an action to recover the insurance.”

V.

**The Court Erred in its Finding of Fact That the Control of the Cotton Company Did Not Pass From West to Sears Until December 1st, 1920.**

**Assignments of Error Nos. 25 and 30.**

There was considerable testimony as to the date when the actual control of the cotton company passed from West to Sears and as to the exact date when the stock certificates in favor of West were cancelled and new certificates issued to Sears. The trial court first fixed the date as of September 1st, 1920, pointing out in its opinion (page 176) that,

“Considering next the evidence as to the transfer of West’s stock to Sears, and its effect upon

the liability of the defendant: Remembering that, as has been already observed, the questions here are to be considered as though the cotton company was the plaintiff, the evidence of West, who was the owner of the cotton company, as to when he transferred his interest to Sears, must be allowed full weight. A different consideration might arise, were this an action by a creditor to enforce a stockholder's liability for corporate debts against West. If West, being the company, declares to the defendant: 'This corporation went under the ownership of Sears at a certain date, and Sears then came into full and complete control' he would announce such a change in the conditions as to make the hazard different from that existing when the insurer made its bond. Furthermore, public policy would not favor the enforcement of a contract which would permit an individual to indemnify himself against his own misconduct."

"West testified that he made the sale of his stock to Sears during the latter part of August. He contended also that it was a part of the agreement of sale that the transfer should be considered as relating back to the month of May, 1920, but I think, the evidence on the subject being considered altogether, the best conclusion that can be made is to fix the date of the transfer at the first of September, 1920. We then must consider that from that date West owned no further interest in the business, and that Sears then became the sole proprietor of it. Therefore, if there exists any liability on the part of the insurer under the bond sued upon, it must be such only as accrued prior to the first of September, 1920."

Later upon further consideration the court changed the date to December 1st, 1920, upon the theory that that was more nearly the date when the transaction between West and Sears was concluded, it being admitted that the promissory note given by Sears to West in payment for the stock bears date December 1st, 1920. All of the testimony on the point as to the transfer of control and ownership is as follows:

Testimony of T. J. West:

"Q. And when did you sell the stock to Mr. Sears?

"A. In the latter part of August, 1922.

"Q. And what, if anything, did you then do with the original certificates issued to you?

"A. Sent them in to the secretary to be transferred." [Tr. p. 380.]

"Q. Now you said it was along about August that you sold out to him?

"A. In the latter part of August, 1920." [Tr. p. 381.]

"At the time I sold my stock to Sears about the last of August, 1920, there was one share of stock left in my name. We had no particular arrangement about it; in fact, nothing was said. Sears gave me a note in payment for the stock which I sold to him. The note didn't come along, however, until in December, 1920. The reason I disposed of my stock was because I had more than I could attend to and Mr. Sears and Mr. McDevitt wished to continue the business, and I gave them a chance to work it out. The prospects were bright and they had a good start. [Tr. pp. 382-383.]



“For the 946 shares of stock I received the note of T. W. McDevitt subsequent to December 1st, 1920. The note was secured by pledge of the 496 shares of stock. I did not receive the pledged stock at the time I received the note. I got the stock before the note was sent to me.” [Tr. p. 388]. The 496 shares of stock were sent through the mail and the note came later. [Tr. p. 388.]

West testified [Tr. pp. 389-390] that between August 25th and September 9th he went to Hartke, who was the secretary of the cotton company, to have the stock transferred and that the transfer was actually made some date between the first and 9th of September 1920 [Tr. p. 389]; that he requested the certificates to be dated back to May 24th. West further testified [Tr. p. 393] that it was his intention to liquidate and close up the cotton company's business at the end of the first year, but that Sears begged him not to do so, and that he then agreed to accept the note of either Sears or McDevitt and sell the stock to Sears, and this discussion took place in the latter part of August, 1920 [Tr. p. 394]; that he told Sears to send the note to him at Calxico and that he, West, then returned to Calxico and secured the certificates standing in his name and sent them in for transfer, and that the new certificates made out in the name of J. B. Sears were sent down to him during the first part of September [Tr. p. 395], and about two weeks after the original certificates were sent in for cancellation; and that he made the sale on the basis of ending of business, April 30th [Tr. p. 395]; and that

he, West, wanted to be relieved of any responsibility for the incoming season's business [Tr. p. 396]; that Mr. Hartke was secretary at the time he sold out to Sears [Tr. p. 396.]

Mr. Norsworthy, the cotton company's bookkeeper, testified that he personally cancelled the old certificates and made out the new certificates to Mr. Sears, but that they were not made out on the date they bear—to-wit, May 24th [Tr. p. 423]; that the actual date of issuance was originally written upon the stocks and certificate and later erased and dated back to May 24th.

Mr. Hartke, who signed as secretary the new certificates issued to Sears, testified [Tr. p. 459] that he had a conversation with West in connection with the transfer of the stock, and that this conversation took place about the 1st day of December, 1920, and that such conversation and the issuance of the stock certificates was some time after December 1st, 1920, and that he, Hartke, was not secretary of the cotton company at the time he signed the certificates, but inasmuch he was secretary on May 24th, the date the certificates bear, he executed them as secretary [Tr. p. 460]; that the date originally entered upon the certificates was December 1st, 1920. [Tr. p. 462].

In addition to the foregoing, the original stock certificates and stock certificate stubs were carefully examined by Milton Carlson, well known handwriting expert, and he testified that the date originally entered upon the stock certificates and upon the stock

certificate stubs and which date was later erased, was November 17, 1920. [See Stipulation p. 478]. Even though the exact date of the transfer of the stock certificates did not occur, and all the details of the purchase of the stock, were not completed, until December 1st, 1920, it is nevertheless respectfully submitted that the control of the cotton company, so far as actual operations of the cotton company's business was concerned, occurred before the cotton company began its second season's operations—to-wit, prior to November 17, 1920. All of the wrongful acts upon which loss is predicated occurred after November 17, 1920. From the foregoing testimony it will be clearly observed that the deal between Sears and West was made on the basis of Sears' taking over the company as of May, 1920, the end of the first cotton season, and that West's intention was that he would not continue the business during the second season; and that he turned over the complete management and control to Sears prior to the time when the second season began. This situation resulted in there being in fact no relationship of employee and employer during the time the alleged losses were sustained and under the law as announced under point V (supra) the destruction of such relationship released the bonding company from all liability for any acts thereafter performed by the "risk."

VI.

**There Was a Breach by the Cotton Company of the Promissory Warranties Made to the Bonding Company and Given as Consideration for the Execution of the Bond, and of the Provisions of the Bond, in That the Cotton Company's Books, Accounts, Stocks and Securities Were Not Inspected and Audited by T. J. West, as Warranted.**

**Assignments of Error Nos. 31, 27, 28, 23, 20 and 2.**

**FACTS**

At the time the bond sued upon was issued the cotton company executed and delivered as part of the consideration for the issuance of the bond answers to certain questions, and expressly agreed as follows:

“It is agreed that the above answers are warranties and constitute the basis of and form a part of the consideration of the bond executed or about to be executed by the Maryland Casualty Company in favor of the undersigned upon the person above named, and also all continuations or renewals thereof or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by the said Company.” [Tr. p. 204].

The bond itself further provides:

“That all statements which the Employer has furnished to the Company concerning the Employee or his duties or accounts are warranted by the Employer to be true;”



One of the warranties made, being paragraph 12 [Tr. p. 202] is as follows:

"12 (a). At what intervals will applicant's books, accounts, stock and securities be inspected and audited and verified with funds on hand or in bank? a. Books checked at least once in every ..... month. Books checked up each month.

"(b). At what intervals and in what manner will outstanding accounts, as shown by applicant's books or reports, be verified? b. We have no such accounts.

"(c). If salesman or collector, how often do you bill the trade direct? c. ....

"(d). By whom will above inspections and audits be made? d. T. J. West Treasurer \* \* \* official capacity."

There is no dispute in the testimony as to what T. J. West did in the way of checking up or examining the books. With the exception of a general statement by the witness, Norsworthy, West's testimony was the only evidence introduced on that question. West testified as follows:

"Q. Did you ever make an examination of his bank account—cash in the bank?

"A. No; only checked the accounts by the statements rendered by the bookkeeper.

"Q. Now what do you mean by that, Just explain to the court so that the court may know what you did in that connection.

"A. There was a statement rendered every month by the bookkeeper which would be sent to all of the officers—or those interested—and outside of going over the purchase and sales accounts, the books were

mere routine; I simply looked at them, without considering them of any particular importance.” [Tr. p. 334.]

“I examined those statements to see what the bank account was—that is all—just to see how it stood. I knew that Mr. Sears died on or about the 1st day of May, 1921. I should say it was about the latter part of March, or, well, sometime in March that I had my first conference with him at which I made the examinations about which I have already testified.” [Tr. p. 334.]

“Q. Now, what books of the company, if any, did you ever examine?

“A. I only was interested in the purchase and sales account of the cotton.

“Q. Well, what particular book did you ever examine?

“A. The cotton account and the acceptance account.” [Tr. p. 337]

“Q. Well, did you examine this acceptance book during the second fiscal year beginning, we will say, September 15, 1920, and thereafter?

“A. Not to the same extent and intensiveness as I did the first year, but enough to see whether they were making money enough to pay me. I was interested to see that, they were making money enough to pay me for my stock that I sold them, and I kept track of it on that basis.

“Q. Well, who pay you?

“A. Mr. Sears.” [Tr. p. 337]

“Q. Now take during the second year, beginning in August or September, 1920, on until Mr. Sears death, and tell the court in detail just what the nature of your examination was of those three books.

“A. Well, we didn’t do any detailed checking, but he would show by the cotton bought and the cotton sold how many bales there would be unsold, and that he had it hedged, and that he would show by his cash account and acceptance account the number of bales on hand and that it corresponded to the acceptances in the bank. That is all the details we would go into.

“Q. Did you personally check the three books you have in your hand?

“A. Not in detail at any time, because they were always in balance. Every night the books would show how many bales of cotton had been bought and sold, and the balance on hand, and the acceptances in the bank would agree with it. If there was any difference I would want to know if they were hedged.

“Q. *Well, did you at any time during the second year of the company’s operations make any independent check for yourself of the books?*

“A. *No, nor the first year either.*

“Q. And did you rely on the statements of Mr. Sears or upon your own investigations? (Italics ours.)

“A. I relied more or less on his statements, and I could see the books for myself—the totals.” [Tr. pp. 337-338]

“A. The bundle of tickets which Mr. Sears showed me were 500. I did not at any time personally check and count the tickets. I did not at any time go to the Citizens National Bank and check the indebtedness of the Cotton Company to the bank, but took the statements as made in the office. I did not have any of these statements which were prepared monthly and mailed to me.

“Q. *Did you ever check or make any audit or check of the books to ascertain whether or not the*

*statements that were being sent to you each month were correct?*

“A. No. I never would have questioned any statements sent out by Sears. (Italics ours.)

“Q. And he, so far as you know, did have on hand at the particular date when he exhibited the tickets to you which he took from the safe, the number of tickets called for by the bought and sold cotton account?

“A. Yes, sir. I didn’t count them, but it looked to be right.

“Q. Did you ever examine this ledger account wherein there appears to be an entry of cotton bought and cotton sold?

“A. No, not that I remember.” [Tr. pp. 339-340.]

“I did not know that the Cotton Company, after it sold the cotton covered by the trust receipts was selling the cotton and putting the outbound documents—that is the drafts drawn on the purchaser of the cotton together with the bill of lading therefor in the checking account of the Citizens National Bank. I thought Sears was taking up acceptances with the proceeds from the sale of the cotton covered by trust receipts. I did not know where he was depositing the money received from the sale of the cotton. I never made any check to ascertain how he was handling the monies realized from the sale of cotton.

“Q. Did you ever go over, while acting as treasurer, and investigate any of the books of the Citizens National Bank or any of the acceptances or records there in the bank?

“A. No; I never went over any records.

“Q. Did you ever look at the check book of the Cotton Company?

“A. No, I never saw a check book.



“Mr. Cosgrove: Do you mean by that check stubs?

“Mr. Parke: Yes, the check stub book.

“Q. Did you ever inquire of Mr. Sears how he was paying the acceptances—that is, in what manner he was paying them?

“A. No, I did not.” [Tr. pp. 341-342.]

“I cannot say whether we had a special expense account in the bank in this particular instance or not. Mr. Sears paid the acceptances during the first year of the Company’s business by checks drawn on the company’s general checking account. I do not know whether he paid operating expenses of the Cotton Company during the first year out of the general checking account or not, as I never checked the books to ascertain that fact.” \* \* \*

“I know the Cotton Company had a class book wherein was listed all cotton by bale number that was purchased and all cotton by bale number that was sold, but I never did look at that book.” [Tr. pp. 334-345]

*“I never at any time compared any of the monthly statements prepared by the bookkeeper with the books of the Cotton Company to ascertain if they were correct and I never went to the plaintiff bank to check as to the amount of cash on hand. (Italics ours.)* I knew in a general way that the books that were kept by the Cotton Company were kept “cotton wise”—that is, that it had a Purchase & Sales book, and Acceptance Account, a Cotton Account, and a bale book, and that they kept these books up.” [Tr. pp. 345-346.]

“I did not at any time make any check of the written statements which were prepared by Mr. Norsworthy, with the books of the company. I did receive and examine, however, a statement showing the transactions of the cotton company’s business for the

first year, but I do not now recall its contents." [Tr. p. 382].

Mr. Norsworthy, who was bookkeeper for the cotton company during the whole period in question testified as follows:

"Mr. West was occasionally in the office of the cotton company, probably once every ten days and he never did, that I know of, make any audit of the books and if he had made such an audit I think I would have known. West never made any examination of the books in my presence." [Tr. p. 422.]

The testimony of Mr. West further shows that during the second season of the cotton companys' operations—that is, from the fall of 1920 until May of 1921, he considered that he had no direct financial interest in the business and was only interested to see whether or not Sears, to whom West had sold all the stock of the corporation, was likely to make sufficient money to pay West for the stock. On this point West testified [Tr. p. 395] that he made the sale of the corporate stock to Sears on the basis of the ending of the business year, April 30, 1920; and again [Tr. p. 396]; that:

"A. And I wanted to be relieved of any responsibility for the incoming season's business. I wanted to withdraw from my responsibility. And we agreed then—

"Q. No, just what was said. Do you mean by 'agreed' that it was stated?

"A. It was stated that we would transfer the stock back then to the end of the business year, and I re-

marked that 'We can't transfer it farther back than where I appeared in a meeting of the board of directors.' So we then went to Hartke and found that it could be transferred as of May 24. We would have transferred it April 30 if we could, at the end of the business year. And then it was done."

"Q. By Mr. Parke: Well, what, if anything, did you do as treasurer after August, 1920?

"Mr. Cosgrove: Now that is susceptible to the same objection.

"Q. By the Court: What did you do acting with the corporation?

"A. I didn't do anything acting with the corporation after 1920.

"Q. By Mr. Parke: After August, 1920?

"A. No."

The learned trial judge in his opinion [Tr. p. 175] properly summarized the situation as regards the examination of the books by West as follows:

"West testified that his investigation of the books only went so far as to give him information as to the purchase and sales account—that is, how much cotton Sears was buying, how much he was selling, and as to whether he was 'hedging' his business

\* \* \*

"Under the representation made by West that he would check the books every month, it became the cotton company's duty not only to report promptly to the bonding company any dereliction of Sears, in the regards specified in the bond, *but upon the occurring of any such dereliction which West would have discovered had he made the inspection of the books and accounts which he agreed to make, the failure to make such inspection and report would exonerate the*



*insurer*; and it must be concluded that if the bonding company might in any event be held responsible for the overdraft of Sears on his personal account, that the cotton company relieved the insurer because it failed in its duty to properly inspect the accounts and make report."

The foregoing constitutes all of the testimony in relation to the examination of the cotton company's books by West, and it is respectfully submitted that such cursory examination of only a portion of the books of the cotton company and no examination at all of the books reflecting the financial condition of the company, or the manner in which its receipts and disbursements were being handled, is a breach of the warranty above set forth.

The fact which may be urged by defendant in error and as indicated by the trial court in its opinion that a checking or auditing of the books might not have disclosed that Sears was improperly applying moneys realized from the sale of cotton which should have been paid to the bank under the trust receipts, does not relieve the cotton company from its obligation to comply with the warranty—that is, have the books checked and audited in accordance with the express agreement. It is not disputed that during both the years of the cotton company's operations substantially all cotton purchased was handled through the plaintiff bank and trust receipts given for the warehouse receipts, and that in no single instance were the "out-bound documents" returned in direct payment or discharge of the trust receipts, but in all cases the pro-



ceeds from the sale of cotton covered by trust receipts was deposited in the general checking account of the cotton company, from which account checks were drawn from time to time in payment and discharge of acceptances and trust receipts, and from this same general checking fund all the operating expenses of the cotton company were paid. A school boy, had he made any check of the books of the cotton company, would have observed these facts. It is not disputed that a complete record of the indebtedness of the cotton company to the bank was kept, and both Mr. Farrar and Mr. Cole, certified public accountants, who testified at the trial, were able by an audit and check of the books to quickly determine that cotton covered by trust receipts held by the plaintiff bank had been sold and the proceeds applied other than in discharge of the trust receipts.

It is respectfully submitted, however, that whether a check or audit might or might not have disclosed any irregularities, the absolute duty rested upon the bonding company to have such check and audit made. The fact that a check or audit is being made regularly in each month often is the controlling influence which prevents a trusted employee from committing irregularities.

The learned counsel for defendant in error urged at the trial in the lower court that under the warranty there was no requirement that an audit or verification of the books and accounts of the cotton company be made, but merely a checking up of the books. It is respectfully submitted that there was not even a

“checking up,” and further that the answer made to the question in warranty No. 12 must be read in the light of the questions and when questions and answers are read together they certainly mean more than that a mere cursory inspection or checking up of one particular phase of the companys’ transactions—that is, cotton bought and sold, would be made. This is all West says he did or intended to do and that this inspection was very perfunctory during the second year. Question and answer (D) states affirmatively that *inspections and audits* will be made by T. J. West. It is not claimed by defendant in error that any audit was made of the stocks and securities, or that there was any attempt made to verify the securities or funds on hand or in bank. During the period when the alleged loss was sustained no check of any of the cotton company’s books was ever made. During all this time West testified that he did not know even where the proceeds from the sale of cotton was being deposited, notwithstanding the fact that full entries of such deposits and of the disposition thereof were fully reflected in the books.

### THE LAW.

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**The Failure of the Cotton Company to Have T. J. West Make a Monthly Examination, Audit and Check of the Books as Agreed Releases the Bonding Company From all Liability.**

In a recent case of Maryland Casualty Company v. Bank of England decided by the Circuit Court of Appeals of the Eighth Circuit and reported in 2 Fed.

(2d Edition) 793, the defense was interposed by the Maryland Casualty Company that the insured had failed to have the books examined as expressly provided in the promissory warranties made by the insured. In that case, question No. 11 contained three questions and answers thereto, as follows:

“In case of applicant handling cash or securities, how often will the same be examined and compared with the books, accounts and vouchers, and by whom? (a) Monthly.

“Will any examination of the applicant’s accounts be made outside of the audit of the state or national bank examiners? (b) No.”

The trial court found that in effect the questions and answers amounted to nothing more than an agreement that the accounts of the insured would be examined by the state bank examiner and that since under the law the state bank examiner was not required to make monthly examinations, the warranties were not breached by the fact that only a yearly examination was made by the state examiner.

The case was reversed on appeal, the Appellate court holding that the second question and answer did not relieve the insured from having its cash and securities examined and compared with the books, accounts and vouchers each month. In passing upon the question, the Appellate court said:

“It is true that it is a rule of construction that ambiguities should be resolved against the drawer of an instrument and that this rule has been properly applied to insurance contracts. American



*Surety Co. v. Pauly*, 170 U. S. 133, 144, 18 S. Ct. 552, 42 L. Ed. 977. However, this does not mean that the contract can be changed or 'refined away' by this mere rule of construction (*Guarantee Co. v. Mechanics' Savings Bank & Trust Co.*, 183 U. S. 402, 419, 22 S. Ct. 124, 46 L. Ed. 253), nor that all other rules of contract construction must stand silent in the presence of this rule. Other rules of construction are that all parts of a contract must be given a reasonable meaning and vitality and that parties are presumed not to insert idle, foolish, meaningless language.

"We think the parties had no difficulty in understanding each other and that, to them, both of the questions and the answers thereto were intended to have the meaning above set forth.

"As the bond expressly provided that it should fail if these monthly comparisons were not made and as they were not made, the bank cannot recover. The difficulty in this, as in some other insurance cases, is that the insured takes the view that all that is necessary to recover on a bond or policy is to pay the premium and suffer a loss. That is rarely the case. The premium is graduated according to the extent of risk as based on experience and reason. The risk of turning a person loose with money without check, word or supervision is one thing, while the risk on the same person under careful, frequent check and supervision is quite another. These promissory obligations of the insured which affect the risk are about the only safeguards the insurer has and cannot be lightly disregarded."



The following cases are also helpful in determining the extent to which the courts require a substantial compliance with a warranty of this character:

United States Fidelity & Guaranty Co. v.  
Downey, 10 L. R. A. (N. S.) 323,

The syllabus is:

“The requirement of an application as to examination of books is not satisfied by accepting as true the amount the employee has in bank as shown by deposit book \* \* \* without any investigation to ascertain from the bank if the statement was true.”

Further continuing the court said:

“The bond provides, among other things, that the Miners’ Union should notify defendant immediately upon discovering any fraud or dishonesty on the part of an employee. The statement made in the application, to the effect, that the accounts of the employee should be examined and verified quarterly, was made for the evident purpose of enabling the guarantor to know what means were to be adopted by the employer to discover fraud or defalcation in the event of its occurrence. It is alleged in the complaint that the shortage of Hogue was not discovered until February 16th, more than two months after the quarterly examination of December 10th. For aught that appears in the testimony, much of this shortage may have existed at the time of the attempted examination of the accounts. This examination was made by two of the trustees according to their own testimony. They made no investigation whatever to ascertain the amount

of money Hogue actually had in the bank, and, in checking up the funds on hand, merely took the balance shown by Hogue's bank book. It needs no argument to show that without such an investigation at the bank there could be no checking up of funds on hand. For anything which the trustees might have known, the cash which they claimed Hogue had on hand might have been drawn from the bank subsequent to the balancing of the bank book, and was not a compliance with the safeguard which the union had agreed to give to the defendant.

"To verify means to prove to be true or correct; to establish the truth of; to confirm. Nothing of this nature was done, or attempted to be done by the trustees, so that there was an absolute breach of the contract made by the union which was the inducement offered defendant for making the bond. The union having failed to do that which it was compelled to do under its agreement, released appellant from all liability under the bond."

Young v. Pacific Surety Co., 137 Cal. 596, the syllabus is:

"Where the applicant for the bond of indemnity represented that the books and accounts of the cashier and bookkeeper could be examined and audited, and all moneys, securities, vouchers, and property on hand would be examined and verified daily, and the applicant, by reason of absence, failed for four days to comply with the terms of the contract, during which time the cashier absconded with his employer's money, such failure discharged the surety from liability upon the bond."

Hunt v. Fidelity & Casualty Co., 99 Fed. 242.

This was a suit upon a policy to indemnify a Fire Insurance Company against loss through embezzlement of an agent. The application for the bond provided that the cash would be compared and verified once a month, and that the statements therein by the terms of the policy "constituted an essential part and formed a basis of the contract." Each month a check was compared and verified with vouchers furnished. During the period of the insurance the company did not at any time compare and verify the cash in the agent's hands, or his bank balance with the accounts kept by him at his office in New York. During the period of the insurance it is found that there was a deficiency in his accounts, and that he had collected and converted money of the company to his own use. Page 244:

"The court below directed a verdict for the defendant upon the ground that it was established that there had been no monthly examination by the assured of the cash and accounts of its agent, in compliance with the promise of the assured.

"Reading the several statements of the assured together, it is plain that the statement that the cash to be compared and verified monthly with accounts and vouchers meant that the assured would monthly examine the accounts and vouchers of its agent, and compare and verify them with the case in his hands, in order to ascertain the correctness of his accounts. Such an examination would have shown what he had received by way of premiums, what he had disbursed by way

of expenses, what he had transmitted to his principal, and how the balance compared with his moneys on hand. A monthly verification of that character would tend to exercise a salutary check upon the transactions of the agent in dealing with the funds of his employer, and might prevent, as well as reveal, any irregularities or dishonest manipulation on his part. It would to some extent, at least, have been a safeguard to the employer and to the insurer, who was to become responsible for any defalcation of the agent."

Page 245:

"The promissory statement, having been made part of the contract between the parties, by the terms both of the policy and the declaration, was, in effect a *warranty* which the assured was bound to fulfil in substance and according to its meaning. *Jeffries v. Insurance Co.*, 22 Wall 53, 22 L. Ed. 833; *Ins. Co. v. France*, 91 U. S. 513, 23 L. Ed. 401; *Brady v. Association*, 9 C. C. A. 252, 60 Fed. 722; *Missouri K. & T. Co. v. German National Bank*, 23 C. C. A. 65, 77 Fed. 117. It is quite immaterial that the statement is not called a warranty. It is a stipulation embodied in the contract, by the words of the policy, for the performance of future acts, and, as such, is an express warranty. *Arn. Ins.* (6th Ed.) 599; *Ang. Ins.* Secs. 140, 141 \* \* \*

"It appeared beyond question upon the trial that its promise to examine its agent's cash monthly had not been fulfilled by the assured. The monthly comparison of the checks sent to it by its agent with the accounts and vouchers sent by him two months previously was not a comparison of the cash in his hands with his re-



ceipts and disbursements, but was merely a comparison of a part of it,—the part which he had transmitted. It did not involve any examination of his accounts in order to ascertain whether his cash on hand corresponded with the premiums received within the last two months. No attempt was made to ascertain this by the assured. What was done was of no value in comparing the cash actually in the agent's hands with the amount which he ought to have on hand at that time. In ruling that the promise of the assured had not been fulfilled, and that the *defendant* was therefore entitled to a verdict, the court below was clearly correct."

Ellzey v. Mass. Bonding & Ins. Co., 142 La. Column 818.

This was a suit upon a fidelity bond guaranteeing the Producers Association against loss in the conduct of its financial affairs by its president. The bond provided that the company would verify the accounts of the president monthly.

On page 820 the court say:

"Before consenting to become surety for Monata, defendant presented to plaintiff association a form of application containing various questions to be answered by it, and the concluding clause of said application contains a stipulation to the effect that the answers are warranted to be true and are conditions precedent to a right of recovery upon the bond applied for, and by the terms of the policy said statement and answers of plaintiff are made part thereof. The answers are to the effect that Monata was to account

monthly to the board of directors, that the books of Monata were to be examined monthly by an auditor or expert accountant, that the funds of the association were to be deposited in the Bank of Hammond and to be withdrawn only by checks signed by Monata and counter-signed by S. B. Ellzey, secretary and treasurer.

“The evidence shows that the bond was given and signed on February 17, 1912, that Monata began his speculations about the 3rd of April, and continued the same until about May 7th, 1912; that the shortage was discovered about the 12th day of May; and that no examination or audit of Monata’s accounts had been made prior to that time.

“The question for decision, therefore, is what is the effect of plaintiff association’s failure to carry out the promises which, in its application for the indemnity bond upon which it sues, it expressly made and warranted, when it stated therein that the accounts of Monata would be checked monthly by the board of directors, and the accounts of Monata would be audited monthly by an expert accountant? The statement thus made in the application is very material to the contract entered into by the defendant, and has a very important bearing upon the risk thus assumed by it. It can be viewed in no other light than a promissory warranty, and the law is explicit that the non-observance of a promissory warranty vitiates the contract. *Hunt v. Fidelity & Gas. Co. of N. Y.*, 39 C. C. A. 496, 99 Fed. 242; *Winkler Brokerage Co. v. Fidelity & Deposit Co. of Maryland*, 119 La. 736, 44 South 449.

“Plaintiff realizing that it had failed to carry out the promises which it made in its application

for the indemnity upon which it now sues, advances in argument the equity of its demand; but we are powerless to assist it in evading or charging the provisions of a contract which it voluntarily entered into, and which constitute the law between itself and defendant.

“It is therefore ordered that the judgment appealed from be set aside and reversed, and plaintiff’s suit dismissed, at its costs in both courts.”

Bank of Cotton Valley v. McInnis, 143 La. Column 436.

This is a suit against the American Bonding Company as surety on a fidelity bond of its cashier, in which case a judgment was rendered against the cashier for the amount of his defalcation. The bond provided “that if the employer, or any of the officers of the employer *became aware* of the employee gambling speculating, etc., the employer shall immediately notify the surety company in writing.” It further provided that the books should be balanced monthly. The bond further provided: Columns 439-440-441:

“‘It is agreed that the above answers shall be warranties, and form a part and be conditions precedent to the issuance, continuance, or any renewal of, or substitution for the bond that may be issued by the American Bonding Company of Baltimore, in favor of the undersigned, upon the person above named.’

“The foregoing questions and answers have been quoted for the reason that each one in turn has been violated by the plaintiff bank; and, as they, under the agreement, are ‘warranties,’ and



form parts of and are made conditions precedent to the issuance, continuance or renewal of, or substitution for, the bond, they have the effect of defeating plaintiff's claim for indemnity.

"As before stated, plaintiff, in its petition, alleges that Mc Innis, while acting as cashier of the bank and in the employ of petitioner, did, during the life of said original bond and continuation certificate defraud your petitioner out of over \$5,000.00 by fraudulent acts and false entries on the books of the bank. Yet, in answer to the question propounded at the time of the issuance of the continuation certificate, the officers of the plaintiff bank answered that McInnis was not indebted to the bank or its officers. Plaintiff seeks to excuse itself on the score of ignorance. But, it was its duty to know the condition of the books of the bank, and to know whether McInnis was indebted to the bank or not. The cash of the bank was not balanced daily, as the bank agreed should be done by McInnis. On the contrary, it went many days, sometimes as many as nine days, without being balanced. It was further stipulated that the loan committee of the bank would examine and compare the books, accounts and vouchers once a month, *which was not done* \* \* \*

"In addition to the small insurance business which plaintiff, said McInnis, was engaged in with its approval, he was also engaged in the cotton business to the knowledge of the officers of the bank. The cotton business was clearly speculative, and it had been stipulated in the bond 'that if the employer, or any of the officers of the employer, become aware of the employee gambling, speculating, etc., \* \* \* the employer



shall immediately notify the surety in writing'. This the employer did not do.

"The statements made by the bank in its application to the bonding company are very material to the contract entered into by it and the defendants, and have very important bearings upon the risk assumed by the latter. They were declared to be warranties, and the non-observance of those warranties vitiated the contract.

"Plaintiff and defendants agreed that the answers to the questions propounded by plaintiff to defendants should be warranties and form parts of and be conditions precedent to the issuance, continuance or any renewal of or substitution for, the bond that was issued by the American Bonding Company of Baltimore in favor of plaintiff.

"It lies within the power of contracting parties to make any matter material to the contract, although such matter may seem to be of little or no value to either party to the contract. When the parties themselves have seen fit to make certain facts the basis of a contract of fidelity insurance the courts will not assume to correct the understanding of the parties as to the materiality of such facts. When the parties have stipulated that a fact is material, the false representation of the existence or non-existence of any such fact will avoid the contract. *Hunt v. Fidelity & Casualty Co.*, 99 Fed. 242, 39 C. C. A. 496; *Willoughby v. Fidelity etc. Co.*, 16 Okla. 546, 86 Pac. 56, 8 Ann. Cas. 609."

*U. S. F. & G. Co. v. Downey*, 38 Cal. 414.

This case again came before the Supreme Court of Colorado in 88 Pacific 451, and the court said:

"A guaranty company gave a bond to a fraternal union to secure the faithful discharge of the duties of its treasurer. The bond provided that the union should notify the company immediately upon discovering any fraud or dishonesty on the part of such officer. In its application, the union stated that the treasurer's accounts would be examined and verified every three months by its board of trustees, and that the business of the union should continue to be managed as above set forth, and it stipulated therein that the answers, statements and representations therein made should be considered warranties. A quarterly examination was made in December, at which time it was found that the treasurer should have had \$740.00 on hand. He submitted a bank book showing deposits of \$440.00, and the balance in cash, but the amount alleged to be in bank was not verified. In February following it was learned that he was short in his accounts. Held, that the union's failure to verify the correctness of the amount of funds in the hands of the treasurer was not a compliance with the safeguard which it had agreed to give the company, and the latter was therefore relieved of liability under the bond."

Pages 418-419:

"For anything which the trustees might have known, the cash which they claimed Hogue had on hand might have been drawn from the bank subsequent to the balancing of the bank book, and therefore, there was not a compliance with the safeguard which the union had agreed to give to the defendant.

“To verify, means to prove to be true and correct, to establish the truth of, to confirm. Nothing of this nature was done or attempted to be done by the trustees, so that there was absolute breach of the contract made by the union, which was the inducement offered the defendant for making the bond. The union having failed to do that which it was compelled to do under its agreement, released appellant from all liability under the bond.”

“The verification of an officer’s accounts, required by his fidelity bond, is not satisfied by accepting as true the amount which he has in bank as shown by his bank pass book, without taking any steps to ascertain from the bank whether or not it represents the true state of the account.”

U. S. F. & G. Co. v. Bank of Batesville, 87 Ark. 348.

The second syllabus is:

“Where, in the application of a policy insuring the fidelity of an employee, the employer represented and warranted that it would check up the employee’s accounts three times a month, and failed to do so, such failure avoided the bond.”

On pages 359-360 the court says:

“No effort was made to ascertain if the money was actually on hand, nor to ascertain in whose possession it was. The plaintiff bank knew that Smith left money with the various subcontractors or deposited it with the local banks most accessible to them, to be used by them in discounting and buying up time checks. No inquiry was ever made, nor report given of the amounts in the

hands of the various subcontractors. Had this been done at stated intervals, the bank could have known in whose hands its money really was, and any mistake made by any of the numerous persons handling the money could have been properly corrected, and no shortage would probably have resulted.

“The questions asked and the answers given in the application for the bond show that it was in the contemplation of the parties to adopt some system whereby the bank should know at frequent intervals the exact state of the accounts between it and the employee, who was the principal in the bond. Evidently this result could not be accomplished, unless the checking up meant not only the examination of the record of the amounts furnished Smith and the time checks remitted by him, but where the money was put out in the hands of numerous persons, as was done in this case, it was also required that the part of the duty of plaintiff bank in checking up the accounts of Smith and requiring of him an account of his handling of the funds once a month would be not only to ascertain the balance that should be on hand but to find out in whose hands it actually was at the time.

“Reversed and dismissed.”

See also:

Garstires v. American Bonding Co., 116 Fed.  
449.



VII.

The Cotton Company Cannot Deny Knowledge of the Performance by Sears of the Acts Done by Him as Secretary and Which It Is Now Claimed Were Dishonest, for the Reason That the Acts Done by Sears Were, as Expressly Plead by Plaintiff, Within the Scope of His Duties as Secretary and Were for the Exclusive Benefit of the Cotton Company in the Prosecution of the Business for Which It Was Incorporated. It Is Not Claimed That Sears Sought to Gain Any Personal Advantage or Benefit to Himself or to Any Other Person Than the Cotton Company.

The Failure of the Cotton Company, Having Knowledge of the Acts of Sears Now Complained of, to Notify the Bonding Company Thereof Within the Time Provided in the Bond, Prevents Any Right of Recovery Thereon and It Estops the Cotton Company From Maintaining Any Action Predicated Upon the Alleged Fraudulent Acts. In View of This Knowledge on the Part of the Cotton Company It Was Error for the Trial Court to Find That Any Fraud or Deceit Was Practised by Sears Upon the Cotton Company.

Assignments of Error 18, 21, 24 and 4 to 17  
Inclusive.

The foregoing proposition is advanced not solely with the view of predicated thereon the defense of

failure on the part of the cotton company to give notice to the bonding company within the time provided in the bond, but also for the purpose of showing that what Sears did was a matter of fact and of law known to and approved of by the cotton company and that the cotton company with this knowledge permitted Sears to continue over a period of a year and a half to operate the company's business in the way and manner now sought to be charged as fraud.

### Facts.

Plaintiff's case is predicated upon the theory that no one save and except Sears took any active part in directing the affairs of the cotton company. Two of the directors, Conduit and Hartke, testified that they took no part whatsoever except to attend directors' meetings, and McDevitt, president, testified that he knew nothing whatsoever of the affairs of the company. West took no part except occasionally to visit the office and examine the cotton record book.

As in this brief before set forth, all matters in relation to the financing of the cotton purchased was left to Sears, but the plan of securing a line of credit from the bank and having the bank pay for cotton, etc., was as outlined in the letter of September 8, 1919, known to and approved of by Mr. McDevitt and Mr. West, and that such plan was the usual and customary way of handling the cotton brokerage business. Furthermore, both McDevitt and West testified [Tr. p. 274 and p. 340] that they knew that Sears was conducting the business in that manner, and that they approved of

that method of doing business. The only thing they objected to was the fact that the money received from the sale of cotton covered by trust receipts was not all applied in discharge of the trust receipts.

It is expressly admitted, however, that the acts of Sears now complained of as fraudulent, were done during the entire first year of the company's operations and at all times during the second year, that is, he always deposited the proceeds for the sale of cotton covered by trust receipts in the general checking account out of which acceptances and general expenses of the cotton company were paid. The books and records of the cotton company without dispute clearly reflect that the business was handled in this manner. An inspection of the cotton company's bank book or check book would have disclosed this fact. At no time does it appear that any inquiry was ever made of Sears by any of the directors as to how he was handling the money received from the sale of the cotton covered by trust receipts, and consequently there were no misrepresentations made to them by Sears in that regard. It is idle to suggest that Sears was moved by some ulterior motive in handling the finances of the cotton company during the second year, since they were handled in identically the same manner as during the first year during which, except for bad loans made with the approval of the other officers of the cotton company, a very substantial profit was made from the buying and selling of cotton.

It must be concluded that if West made any examination of the cotton company's books, they met with



his approval, for we find no record of any complaint being made. He, West, testified [Tr. p. 345] that they appeared to be kept properly, and Mr. Norsworthy testified [Tr. p. 403] that they were kept in all respects similar to the books kept by McFadden & Company, cotton brokers, and were full and complete. Mr. Farrar, certified public accountant, testified [Tr. p. 442] that the books were full and complete and after Sears' death balanced within 10¢. There was a dispute between the auditor who testified on behalf of the plaintiff in error and the auditor who testified on behalf of the defendant in error as to whether or not a cotton trust account covering the liability of the cotton company to the bank for warehouse receipts entrusted to it, should have been set up in the books. The auditor for the defendant in error believes such an account should have been set up, while Mr. Farrar, auditor for the plaintiff in error, and Mr. Norsworthy, the bookkeeper, both testified that in their opinion, such an account was not necessary to reflect the true financial condition of the cotton company, and Mr. Norsworthy testified [Tr. p. 412] that he had been the bookkeeper for, and had audited a great many sets of cotton brokerage books, and had never seen such an account set up. If such an account was necessary such fact would have been apparent to Mr. West had he examined the books, but no complaint was made.

It is respectfully submitted that the evidence does not warrant the finding of the trial court that Sears wilfully falsified the books and records of the cotton company.



In brief, the record discloses that everybody concerned—that is, the officers of the bank and the officers of the cotton company, knew and approved of everything that was done by Sears on behalf of the cotton company except the manner in which the proceeds for the sale of cotton were disbursed. The books and records of the cotton company and the large number of transactions aggregating more than a million dollars, carried on between the cotton company and the bank, clearly reflected and brought home to each corporation full knowledge of the manner in which the funds of the cotton company, realized from the sale of cotton, were being disbursed,—to-wit, that such proceeds from cotton covered by trust receipts was being commingled with other funds in the general checking account and disbursed for all purposes of the cotton company, including the payment of acceptances and outstanding trust receipts and general operating expenses. As to all transactions had with the bank by Sears acting as secretary for the cotton company, both the cotton company and the bank are bound to know the facts when those transactions were in the regular course of the cotton company's business and of the bank's business and for their use and benefit and transacted by their corporate officers within the scope of their duties, and not for the personal gain or advantage of the officers transacting the business.

## THE LAW.

---

Since the Cotton Company, Insured, Became a Corporation Sole—To-wit, J. B. Sears, on December 1st, 1920, It Must Be Charged With Full Knowledge of All of the Acts Thereafter Performed by J. B. Sears. It Was the Duty, Therefore, of the Cotton Company, Having Such Knowledge, to Promptly Report to the Bonding Company the Acts Upon Which Loss Is Now Predicated. No Report Was Made Until July, 1921, or a Period Far Beyond That Expressly Provided in the Bond. Such Failure to Notify the Bonding Company Released the Bonding Company From Liability.

Furthermore, It Cannot Be Said That the Cotton Company Did Not at All Times Prior to the Date When It Became a Corporation Sole—To-wit, J. B. Sears, Have Knowledge of the Acts Being Performed by J. B. Sears and Which It Is Now Claimed Were Wrongful.

In the case of *Davies & Co. v. Porter*, 248 Fed. 397 (Circuit Court of Appeals, Eighth Circuit), suit was brought by Porter, the plaintiff below, as receiver of the elevator company, to recover money paid to Davies, the defendant below, by one A. J. Norby, which money belonged to the elevator company, as was well known to Davies & Co., the defendant, and was used for alleged wagering transactions. The question was: "Were Norby's transactions with the defendant for

*himself or (as general manager of the elevator company) for the elevator company and its sole benefit?"*

The undisputed evidence shows that the elevator company was a South Dakota corporation; that the directors were Mr. Porter, president; Mr. McNulty, vice-president; and *Mr. Norby, secretary and general manager.* (THIS WAS EXACTLY SEARS' POSITION IN THE CASE AT BAR.)

The company transacted its business through Norby, who had sole charge of it in Minneapolis. The management of the company's business in Minneapolis was left entirely in charge of Norby. The other directors but rarely visited that office and never examined its books. The checks were given in all transactions, most of them drawn by Norby, as secretary, and some by Miss Baker, the bookkeeper, at the request of Norby. (*Miss Baker occupied the position of Norworthy in the case at bar, drawing checks at the request of Sears.*)

On pages 400-401. the court say:

"During the time these transactions took place, the defendant paid to Norby at different times, as profits, sums amounting to \$19,444.94, all of which was paid by checks payable to Norby, and by him deposited to the credit of the elevator company and credited on its books. Had the directors, or either of them, examined the books of the company, they would have learned of these transactions and that they were for the sole benefit of the company. *From a careful reading of the testimony it is impossible to escape the conclusion*

*that it establishes conclusively that Norby's transactions were for the sole use and benefit of the company, and that were carried on in his name, and for the only reason that the membership in the Chamber of Commerce was in his name. The neglect of the other directors, who were the sole stockholders, besides Norby and his wife, to examine the books of the corporation for years, which would have shown these transactions, and failing to make any effort whatever to ascertain how the business of the company was being conducted by Norby, was not only a breach of their duties as directors, but also, as by the exercise of any diligence whatever, they could have ascertained the facts, they must be held to have knowledge of them. Gold Mining Co. v. National Bank, 96 U. S. 640, 24 L. Ed. 648; Rolling Mill v. St. Louis etc. Co., 120 U. S. 256, 7 Sup. Ct. 542, 30 L. Ed. 639; Pittsburg etc. Co. v. Keokuk, 131 U. S. 371, 9 Sup. Ct. 770, 33 L. Ed. 157. In Brown's Valley State Bank v. Porter, 232 Fed. 434, 146 C. C. A. 428, an action arising out of similar transactions of Norby as general manager of the elevator company, in which the evidence was very much like that in this case, we held that his acts were those of the corporation."*

\* \* \* \* \*

"The court erred in refusing to direct a verdict in favor of the defendant, and the cause is reversed and remanded, with directions to grant a new trial."

*McCaskill v. U. S.*, 216 U. S. 504. In that case suit was brought by the United States to cancel a patent to land to W. J. Ward and a deed to McCaskill



Company upon the ground that his proof was fraudulent and untrue. The land was conveyed by Ward to McCaskill & Company, the copartnership. They afterwards incorporated the McCaskill Company and deeded the land to said company. The answer alleged that the McCaskill Company was a *bona fide* purchaser.

On page 514 the court say:

“Does applicant occupy the position of the innocent purchaser, and is the Government precluded from receiving the relief prayed for in the bill, because of such fact? The answer to the question depends upon a proposition of law, and whether J. J. McCaskill had knowledge of the fraudulent acts of Ward. This knowledge was, in effect, found, by both the lower courts, and, giving to their finding the strength that should be accorded to it, we pass to the consideration of the proposition of law that the knowledge of J. J. McCaskill, though president of the McCaskill Company, cannot be imputed to it. because, as appellant’s argument is, while the knowledge of an agent is the knowledge of the principal, an ‘exception to the rule is that if the agent is acting in a matter in which he has a personal interest, or in communication with which he is interested with a third person, the presumption is that he will not communicate the facts in controversy,’ and it is urged that ‘the rule should be rigidly applied in cases of fraud or torts.’ For these propositions, appellant cites *Clark v. Metropolitan Bank*, 3 Duer (N. Y.) 241; *Frenkel v. Hudson*, 82 Ala. 162; *Allen v. South. P. R. R. Co.*, 150 Mass. 200;

Innerarity v. Mer. Nat. Bk., 139 Mass. 332; Atlantic Nat. Bk. v. Harris, 118 Mass. 147; Loring v. Brodie, 134 Mass. 453; Hightstown v. Christopher, 40 N. J. L. 435.

“Undoubtedly a corporation is, in law, a person or entity entirely distinct from its stockholders and officers. It may have interest distinct from theirs. Their interests, it may be conceived, may be adverse to its interest, and hence has arisen against the presumption that their knowledge is its knowledge, the counter presumption that in transactions with it when their interest is adverse and knowledge will not be attributed to it. But while this presumption should be enforced to protect the corporation, it should not be carried so far as to enable the corporation to become a *means of fraud* or a *means to evade its responsibilities*. A growing tendency is therefore exhibited in the courts to look beyond the corporate form to the purpose of it and to the officers who are identified with that purpose. Illustrations are given of this in Cook on Corporations, sections 663, 664 & 727. The principle was enforced in this court in Simmons Creek Coal v. Doran, 142 U. S. 417. In that case a corporation claimed title to land through a deed of its corporators, one of whom became its president. Of the effect of this, the court said: ‘Associated together to carry forward a common enterprise, the knowledge or actual notice of all these corporators, and the president was the knowledge or notice of the company, and if constructive notice bound them, it bound the company.’”

In the case of Phillips v. U. S. F. & G. Co., 193 New York Supplement, 468, the plaintiff was liquidator

of the New York National Insurance Company and sought recovery upon a depository bond issued by the defendant. It appears that James J. Boland was president of the James J. Boland Company, which, in fact, was the owner of and controlled the New York National Insurance Company. It was he who applied to the defendant for the depository bond. At the time the application was made, he knew that the risk, to-wit, the North Penn Bank, was insolvent. The bond guaranteed the re-payment by the bank of all moneys deposited with it. The court held that the knowledge of Boland while acting within the scope of his duties and for the benefit of the New York National Insurance Company (insured) was the knowledge of the insured; that since the insured had knowledge of facts which it concealed from the surety company there was no liability. On page 482 the court said.

“James J. Boland, the president of James J. Boland Company, which, as the general agent of the N. Y. National and The Seneca Fire Insurance Companies, had in charge the procurement of depository bonds for these companies, himself directed the procurement of the bond now in suit, and the bond of the Maryland Casualty Company issued on May 26th. James J. Boland, as before related, was also the president of the N. Y. National and The Seneca Fire Insurance Companies. The N. Y. National and The Seneca Fire Insurance Companies paid no premiums, made no contracts and procured no bonds unless James J. Boland, their president and the president of their general agent, was present when the bonds were



obtained; in effect, the very corporations which he represented. There is not here presented, therefore, the question as to when the knowledge of an agent is attributable to the principal in reference to transactions performed on behalf of the principal by an agent other than the one having knowledge. These corporations acted to obtain bonds only if the acts of James J. Boland were corporate acts. *If James J. Boland was the corporation which obtained the bonds, then the knowledge possessed by him when he obtained them was corporate knowledge.* The authorities are clear upon this point. *Holden v. N. Y. & Erie Bank*, 72 N. Y. 286; *Taylor v. Commercial Bank*, 174 N. Y. 181, 66 N. E. 726, 62 L. R. A. 783, 95 Am. St. Rep. 564; *Rocky River Development Co. v. German American Brewing Co.*, 193 App. Div. 197, 184 N. Y. Supp. 155.”

Page 483:

“In our case the James J. Boland Company and its directors were not acting for themselves in procuring these bonds, but for their insurance companies, which, under all the authorities are therefore chargeable with the knowledge possessed by them.”

The Appellate Court reversed the judgment against the Surety Company.

*Fairchild v. McMahon*, 139 N. Y. 290. The second syllabus is:

“All persons who seek for or in the name of the owner in bringing about the transaction must be deemed his agents, where he accepts the fruits



of their efforts, and all the methods employed by them are imputable to him; he may not even, though innocent, receive and recover upon a security given on the sale and at the same time disclaim responsibility for the fraud by means of which the purchaser was induced to deliver it."

Blood v. La Serena Land & Water Co., 134 Cal. 361. On page 370, the court say:

"Whether all the shareholders knew of the commission paid Blood, Jr., is immaterial. If the directors had knowledge at the time the mortgage was authorized by them, or if the president and secretary of the corporation had such knowledge when they executed the mortgage, the corporation is chargeable with the knowledge. The rule of law seems to be, that notice to the individual shareholders is not binding upon the corporation as a collective body; but *notice to its corporate agents, who have authority to represent the whole company*, is notice to the corporation. (1 Morawetz on Private Corporations, Secs. 540b, 540c. See cases collected in note to *Bank of Pittsburgh v. Whitehead*, 10 Watts, 397, in 36 Am. Dec. 186, 188-200.)"

McKenney v. Ellsworth. 165 Cal. 326. The first syllabus is:

"The general rule, that where an agent of a corporation is dealing with the corporation in a transaction in his own behalf, it will not be presumed that he will communicate to his principal facts affecting the transaction, is subject to the exception that if the agent is in fact acting for his principal in the transaction, even though he

may have an opposing personal interest, it is his duty, notwithstanding his interest, to communicate to his principal any facts in his possession, material to the transaction, and the law will therefore presume, in favor of third persons, that he made such communication.”

The position of defendant that the insured cannot recover because it knew of and permitted the continuance of alleged wrongful acts by its managing agent performed in the conduct of its business and for its benefit, is merely a corollary to the other principal point urged by the defendant that the Cotton Company cannot recover for the acts of Sears done within the scope of his duties as its managing agent and for its exclusive benefit and where it, the Cotton Company, received all the benefits and therefore sustained no loss.

Upon the whole case it is very earnestly submitted that in the interests of justice to this plaintiff in error the judgment should be reversed.

Dated, Los Angeles, California, September 15, 1925.

Respectfully submitted,

W. S. BICKSLER,

W. C. SMITH,

DALE H. PARKE,

*Attorneys for Plaintiff in Error.*



No.

4635

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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MARYLAND CASUALTY COMPANY, a Cor-  
poration,

Plaintiff in Error,

vs.

THE CITIZENS NATIONAL BANK OF LOS  
ANGELES, a Banking Corporation,

Defendant in Error.

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Transcript of Record.

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Upon Writ of Error to the United States District  
Court, for the Southern District of Cal-  
ifornia, Southern Division.

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No.

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United States  
Circuit Court of Appeals  
For the Ninth Circuit.

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MARYLAND CASUALTY COMPANY, a Corporation,

Plaintiff in Error,

vs.

THE CITIZENS NATIONAL BANK OF LOS ANGELES, a Banking Corporation,

Defendant in Error.

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Upon Writ of Error to the United States District Court, for the Southern District of California, Southern Division.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italics* the two words between which the omission seems to occur.]

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**Names and Addresses of Attorneys:**

For Plaintiff in Error:

BICKSLER, SMITH & PARKE, Esqs., Citizens  
National Bank Building, Los Angeles, California.

For Defendant in Error:

HUNSAKER, BRITT & COSGROVE, Esqs.,  
Title Insurance Building, Los Angeles, California.



United States of America, ss.

The President of the United States of America,

To the Judges of the District Court of the United States, for the Southern District of California,

GREETING:

Because in the record and proceedings, and also in the rendition of the judgment of a plea which is in the said District Court, before you between THE CITIZENS NATIONAL BANK OF LOS ANGELES, a Banking Corporation, plaintiff, and MARYLAND CASUALTY COMPANY, a Corporation, defendant, a manifest error hath happened, to the great damage of the said MARYLAND CASUALTY COMPANY, a Corporation, defendant, as by its complaint appears, and it being fit, that the error, if any there hath been, should be duly corrected, and full and speedy justice done to the parties aforesaid in this behalf, you are hereby commanded, if judgment be therein given, that then, under your seal, distinctly and openly, you send the record and proceedings aforesaid, with all things concerning the same, to the United States Circuit Court of Appeals for the Ninth Circuit, together with this writ, so that you have the same at the City of San Francisco, in the State of California, on the 4th day of August, 1925, next, in the said United States Circuit Court of Appeals, to be there and then held, that the record and proceedings aforesaid be inspected, the said United States Circuit Court of Appeals may cause further to be done therein to correct that error, what of right and according to the law and custom of the United States should be done.

WITNESS, the HON. William Howard Taft, Chief Justice of the United States, this 6th day of July, in the year of our Lord one thousand nine hundred and twenty-five and of the Independence of the United States the one hundred and fiftieth.

Chas. N. Williams

Clerk of the District Court of the United States  
of America, in and for the Southern District  
(Seal) of California.

The above writ of error is hereby allowed.

Wm P James

Judge .

I hereby certify that a copy of the within Writ of Error was on the 6th day of July, 1925, lodged in the office of the Clerk of the said United States District Court, for the Southern District of California, Southern Division, for said Defendants in Error.

Chas. N. Williams

Clerk of the District Court of the United States  
for the Southern District of California.

[Endorsed]: United States Circuit Court of Appeals for the NINTH CIRCUIT MARYLAND CASUALTY COMPANY, a Corporation, Plaintiff in Error vs. THE CITIZENS NATIONAL BANK OF LOS ANGELES, Defendant in Error Writ of Error Filed July 6—1925 Chas N Williams Clerk  
R S Zimmerman deputy

United States of America, ss.

To THE CITIZENS NATIONAL BANK OF LOS ANGELES, Greeting:

You are hereby cited and admonished to be and appear at a United States Circuit of Appeals for the Ninth Circuit, to be held at the City of San Francisco, in the State of California, on the 4th day of August, A. D. 1925, pursuant to a Writ of Error filed in the Clerk's Office of the District Court of the United States, in and for the Southern District of California, in that certain action wherein MARYLAND CASUALTY COMPANY, a Corporation, is plaintiff in error and you are Defendant in error to show cause, if any there be, why the judgment rendered against said plaintiff in error as in the said Writ of Error mentioned, should not be corrected, and speedy justice should not be done to the parties in that behalf.

WITNESS, the Honorable Wm P. James United States District Judge for the Southern District of California, this 6th day of July, A. D. 1925, and of the Independence of the United States, the one hundred and fiftieth.

Wm P James

U. S. District Judge for the Southern District  
of California.

Receipt of Copy of foregoing Citation is hereby admitted this 6th day of July 1925

Hunsaker, Britt & Cosgrove

Attys for Plaintiff

[Endorsed]: 1124 IN THE UNITED STATES  
CIRCUIT COURT OF APPEALS FOR THE

NINTH CIRCUIT MARYLAND CASUALTY  
COMPANY, a Corporation, *Plaintiff*, vs. THE CITI-  
ZENS NATIONAL BANK OF LOS ANGELES,  
*Defendant*. Citation FILED JUL 7 1925 CHAS.  
N. WILLIAMS, Clerk By L. J. Cordes Deputy Clerk.

IN THE SUPERIOR COURT OF THE STATE  
OF CALIFORNIA, IN AND FOR THE  
COUNTY OF LOS ANGELES

THE CITIZENS NATIONAL )	No. 106090
BANK OF LOS ANGELES, )	
Plaintiff, )	PETITION FOR
—vs— )	REMOVAL FOR
MARYLAND CASUALTY )	DIFFERENCE
COMPANY, a Corporation, )	OF
Defendant. )	CITIZENSHIP.

---

Now comes defendant, and respectfully represents  
to this Honorable Court:

I.

That at all of the times herein alleged plaintiff was,  
and now is, a National Banking Corporation or As-  
sociation organized and existing under the laws of  
the United States, and pursuant to, and by virtue of  
the Federal Statutes in such case made and provided,  
is a citizen and resident of the State of California.

II.

That defendant herein, at all of the times herein  
alleged was, and now is a corporation organized and  
existing under and pursuant to the laws of the State  
of Maryland, and a citizen and resident of the State  
of Maryland, with its principal place of business in



the City of Baltimore, State of Maryland, and is a non-resident of the State of California.

III.

That the amount in dispute in the above entitled action is the sum of \$50,000.00, exclusive of interest and costs.

IV.

That the controversy in this action and at the time of the commencement of said action, and at all of the times herein alleged was, and now is, between citizens of different states, to-wit: Between the plaintiff, a citizen and resident of the State of California, and the defendant, a citizen and resident of the State of Maryland.

V.

That defendant desires and requests the suit herein to be removed to the United States District Court, in and for the Southern District of California, Southern Division, and herewith offers a good and sufficient bond in the sum of \$500.00 upon its entering in said United States District Court, Southern District of California, Southern Division, thirty (30) days from the filing of this petition, a certified copy of the record in this suit and for the payment of all costs that may be awarded by the aforesaid United States District Court, if said Court shall hold that this suit was wrongfully or improperly removed thereto.

WHEREFORE, petitioner prays that this Honorable Court proceed no further herein; that it make and duly enter an order for the removal of this suit, as required by law, and to accept the said surety bond

filed herein, and cause the record herein to be removed into said United States District Court, Southern District of California, Southern Division, and for such other and further order as defendant may in law and equity be found entitled.

MARYLAND CASUALTY COMPANY.

By E. F. KRAEMER

Manager So-Calif Claim Div

BICKSLER, SMITH & PARKE

Attorneys for Defendant.

STATE OF CALIFORNIA, County of Los Angeles, ss.

E. F. KRAEMER being by me first duly sworn deposes and says: that he is the agent and manager of Defendant Corporation, in the above entitled action; that he has heard read the foregoing Petition for Removal and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information or belief and as to those matters that he believes it to be true.

That no officer of defendant corporation is within the jurisdiction of the Court; and that affiant is duly authorized herein

E. F. KRAEMER

Subscribed and sworn to before me this 27th day of May, 1922.

W. C. SMITH

Notary Public in and for the County of Los Angeles,  
State of California (Seal)

[Endorsed]: (Copy) No. 106090 Dept. . . . .  
 IN THE SUPERIOR COURT In and for the County  
 of Los Angeles, STATE OF CALIFORNIA,  
 THE CITIZENS NATIONAL BANK OF LOS  
 ANGELES, Plaintiff vs. MARYLAND CASUALTY  
 COMPANY, a Corporation, Defendant PETITION  
 FOR REMOVAL FOR DIFFERENCE OF CITI-  
 ZENSHIP. FILED 1922 MAY 31 A M 9 41 L. E.  
 LAMPTON, County Clerk By I. Moore Deputy.  
 Received copy of the within Petition this 27th day  
 of May 1922 HUNSAKER, BRITT & COSGROVE  
 Attorney for Plaintiff. BICKSLER, SMITH &  
 PARKE 829 Citizens Nat'l Bank Bldg. Fifth &  
 Spring Sts. Los Angeles. Cal. Telephones: 10227;  
 Main 5166 Attorneys for Defendant.

IN THE SUPERIOR COURT OF THE STATE  
 OF CALIFORNIA, IN AND FOR THE  
 COUNTY OF LOS ANGELES.

THE CITIZENS NATIONAL )	No. 106090
BANK OF LOS ANGELES, )	
Plaintiff, )	NOTICE OF
—vs— )	MOTION FOR
MARYLAND CASUALTY )	HEARING PETI-
COMPANY, a Corporation, )	TION FOR
Defendant. )	REMOVAL.

To The Citizens National Bank of Los Angeles,  
 Plaintiff:

To Messrs. Hunsaker, Britt & Cosgrove, Attorneys  
 for Plaintiff:

You and each of you will take notice that the Mary-  
 land Casualty Company, a corporation, defendant

named herein, will, on Thursday, June 1st, 1922, at ten o'clock A. M. of said day, in Department 16 of said Court, move and petition said Superior Court for the removal of the above entitled cause to the United States District Court in and for the Southern District of California, Southern Division, upon the following grounds:

1. That said Maryland Casualty Company, named defendant herein, is a corporation organized under the laws of the State of Maryland, and a citizen and resident of the State of Maryland, and that plaintiff is a National Banking Association organized under the laws of the United States and under and pursuant to the law of the United States is a citizen and resident of the State of California; that therefore said petition for removal is based upon the ground of diverse citizenship.

2. Said motion will be based upon the record, files and proceeding of said cause, and upon the petition for removal served and filed herein, together with a good and sufficient bond in the sum of \$500.00, as provided by statute, which said bond defendant will ask said Court to prove at said time.

3. And defendant shall, at said time, ask for such other and further relief as it may in law and equity be found entitled.

Dated—May 27th, 1922.

BICKSLER, SMITH & PARKE

Attorneys for Defendant.



[Endorsed]: (COPY) No. 106090 Dept 16  
 IN THE SUPERIOR COURT In and for the County  
 of Los Angeles. STATE OF CALIFORNIA, THE  
 CITIZENS NATIONAL BANK OF LOS AN-  
 GELES, Plaintiff vs MARYLAND CASUALTY  
 COMPANY, a Corporation, Defendant NOTICE  
 OF MOTION FOR HEARING PETITION  
 FOR REMOVAL. FILED 1922 MAY 31 A M  
 9 41 L. E. LAMPTON, County Clerk By I. Moore  
 Deputy Received copy of the within Notice this 27th  
 day of May 1922 HUNSAKER, BRITT & COS-  
 GROVE Attorney for Plaintiff. BICKSLER, SMITH  
 & PARKE, 829 Citizens Nat'l Bank Bldg. Fifth &  
 Spring Sts. Los Angeles, Cal. Telephones: 10227;  
 Main 5166 Attorneys for Plaintiff.

IN THE SUPERIOR COURT OF THE STATE  
 OF CALIFORNIA, IN AND FOR THE  
 COUNTY OF LOS ANGELES.

THE CITIZENS NATIONAL )	No. 106090
BANK OF LOS ANGELES, )	
Plaintiff, )	BOND ON RE-
—vs— )	MOVAL TO
MARYLAND CASUALTY )	UNITED STATES
COMPANY, a Corporation, )	DISTRICT
Defendant. )	COURT.

KNOW ALL MEN BY THESE PRESENTS:

That the Fidelity & Deposit Company of Maryland,  
 a corporation organized and existing under and by  
 virtue of the laws of the State of Maryland and hav-  
 ing authority to transact business pursuant to the Acts  
 of Congress in such case made and provided, to-wit:

“Acts relative to the cognizances, stipulations, bonds and undertakings, and to allow certain corporations to be accepted as surety therein” is held and firmly bound unto the Citizens National Bank, a Corporation, plaintiff herein, in the sum of Five Hundred Dollars (\$500.00) for the payment of which well and truly to be made unto said plaintiff and its assigns, the said Fidelity & Deposit Company of Maryland binds itself, its successors and assigns jointly and firmly by these presents; upon condition, nevertheless, that:

WHEREAS, the above named Citizens National Bank has heretofore brought a suit of a civil nature in the Superior Court of the County of Los Angeles, State of California, against the said Maryland Casualty Company, a corporation, organized under the laws of Maryland, and a citizen and resident of Maryland; and,

WHEREAS, the said Maryland Casualty Company, a Corporation, simultaneously with the filing of this bond intends to and will file its petition in said suit in the State Court for the removal of this suit into the United States District Court in and for the Southern District of California, Southern Division, in the district where such suit is now pending, to-wit: The Superior Court within and for the County of Los Angeles, State of California, pursuant to and in accordance with the provisions of the Act of Congress in such case made and provided.

NOW THEREFORE, the condition of this obligation is such that if the said defendant and petitioner herein, Maryland Casualty Company, a corpora-

tion, shall enter in the said United States District Court in and for the Southern District of California, Southern Division, within thirty (30) days from the filing of this petition, a certified copy of the record of said suit in said Superior Court, and shall well and truly pay all costs that may be awarded by the said United States District Court, as aforesaid, if said Court shall hold that said suit was wrongfully or improperly removed thereto, then this obligation shall be void, but otherwise shall remain and be in full force and virtue.

IN WITNESS WHEREOF, the said Fidelity & Deposit of Maryland, has caused these presents to be signed by R. W. Stewart, and attested by C. M. Evarts, and its corporate seal to be hereunto affixed this 27th day of May, 1922.

FIDELITY AND DEPOSIT COMPANY  
of MARYLAND

By R. W. Stewart

Attorney-in-Fact.

C. M. Evarts

(SEAL) Agent

Approved June 1-22

CHAS S. CRAIL

Judge

STATE OF CALIFORNIA, County of Los Angeles ss

On this 27th day of May 1922, before me, I. C. SWAIN, a Notary Public, in and for the County and State aforesaid, duly commissioned and sworn, per-

sonally appeared R. W. Stewart and C. M. Evarts known to me to be the persons whose names are subscribed to the foregoing instrument as the Attorney-in-Fact and agent respectively of the Fidelity and Deposit Company of Maryland and acknowledged to me that they subscribed the name of Fidelity and Deposit Company of Maryland thereto as principal and their own names as Attorney-in-Fact and Agent, respectively.

(SEAL)

I. C. SWAIN

Notary Public in and for the State of California,  
County of Los Angeles.

[Endorsed]: (COPY) No 106090 Dept.....  
IN THE SUPERIOR COURT In and for the County  
of Los Angeles. STATE OF CALIFORNIA, CITI-  
ZENS NATIONAL BANK OF LOS ANGELES,  
Plaintiff vs. MARYLAND CASUALTY COMPANY,  
a Corporation, Defendant BOND ON REMOVAL TO  
UNITED STATES DISTRICT COURT. FILED  
1922 MAY 31 A M 9 41 L. E. LAMPTON, County  
Clerk By I. Moore, Deputy BICKSLER, SMITH  
& PARKE, 829 Citizens Nat'l Bank Bldg. Fifth &  
Spring Sts. Los Angeles, Cal. Telephones: 10227;  
Main 5166 Attorneys for Defendant.



IN THE SUPERIOR COURT OF THE STATE  
OF CALIFORNIA, IN AND FOR THE  
COUNTY OF LOS ANGELES.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES,) No. 106090	
Plaintiff )	ORDER REMOV-
—vs— )	ING CASE TO
MARYLAND CASUALTY )	UNITED STATES
COMPANY, a Corporation, )	COURT.
Defendant. )	

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This cause coming on to be heard upon the motion and petition of defendant for the removal of the above entitled cause to the United States District Court, in and for the Southern District of California, Southern Division; no one appearing as counsel for plaintiffs, and Messrs. Bicksler, Smith & Parke appearing as counsel for defendant, the same was argued and submitted to the Court for its determination; and the Court being fully advised in the premises, considered said petition and motion well taken, and said petition and motion are hereby granted.

IT IS THEREFORE ORDERED that said cause be, and the same is hereby transferred to said United States District Court, in and for the Southern District of California, Southern Division, for further proceedings according to law, a bond of the Fidelity & Deposit Company of Maryland in the sum of \$500.00 having been duly filed, which is hereby approved.

Dated—June 1st, 1922.

CHAS S. CRAIL

Judge of the Superior Court of Los Angeles  
County, Cal. Department No. 16.

[Endorsed]: (COPY) No. 106090 Dept.....  
IN THE SUPERIOR COURT OF THE STATE  
OF CALIFORNIA, In and for the County of Los  
Angeles. THE CITIZENS NATIONAL BANK OF  
LOS ANGELES, Plaintiff vs. MARYLAND CAS-  
UALTY COMPANY, a Corporation, Defendant  
ORDER REMOVING CASE TO UNITED  
STATES COURT FILED JUN 1 1922 L. E.  
LAMPTON, County Clerk By Roy Goff, Deputy.  
BICKSLER, SMITH & PARKE 829 CITIZENS  
NAT'L BANK BLDG. FIFTH & SPRING STS.  
LOS ANGELES, CAL. TELEPHONE 10277;  
MAIN 5166 Attorneys for Defendant.

[Endorsed]: No. 1124 Civil United States Dis-  
trict Court Southern District of California The  
Citizens National Bank of Los Angeles plaintiff vs  
Maryland Casualty Co Defendant Certified Record  
on Removal FILED JUN 9 1922 CHAS. N. WIL-  
LIAMS, Clerk, By Edmund L. Smith Deputy Clerk

IN THE SUPERIOR COURT OF THE COUNTY  
OF LOS ANGELES, STATE OF  
CALIFORNIA.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES, )	
Plaintiff, )	
vs. )	
MARYLAND CASUALTY )	COMPLAINT.
COMPANY, )	
Defendant. )	

---

Plaintiff, The Citizens National Bank of Los An-  
geles, for cause of action against the defendant, al-  
leges:—

1. That at all the times herein mentioned, the plaintiff was and is now a banking association duly incorporated and existing under and by virtue of the laws of Congress of the United States of America, and having its principal place of business in the city of Los Angeles, state of California.

That at all the times herein mentioned, the defendant was and is now a corporation organized and existing under and by virtue of the laws of the state of Maryland, and duly authorized by the state of California to act as surety upon bonds and undertakings, including fidelity bonds of employes; and during all of said times was and yet is transacting business as such surety in said state of California.

2. That at all the times herein mentioned California Cotton & Factorage Company was a corporation duly organized and existing under and by virtue of the laws of the state of California, having its principal place of business at the city of Los Angeles, in said state, and was engaged in the business of buying, selling, handling and dealing in cotton and all the bi-products thereof, and during all of said time one J. B. Sears was the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company.

3. That on or about the 26th day of December, A. D. 1919, the defendant herein executed and delivered to said California Cotton & Factorage Company a certain fidelity bond or policy of fidelity and guaranty insurance, wherein and whereby said Maryland Casualty Company, in consideration, among others,

of a cash premium, then and there paid to and received by it from said California Cotton & Factorage Company, and the annual payment thereafter in advance of the yearly premium upon said bond, agreed to reimburse said California Cotton & Factorage Company for any loss, not exceeding fifty thousand dollars (\$50,000.00), of money, securities or other personal property, including that for which said California Cotton & Factorage Company might be responsible to others, which said California Cotton & Factorage Company might sustain by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication on the part of said J. B. Sears, while in the performance of his duties as secretary of said California Cotton & Factorage Company. That a copy of said bond, with the indorsements thereon, is in the words and figures as follows, to wit:—

“Register No. 5493. (\$2.50 cancelled revenue stamps attached)

MARYLAND CASUALTY COMPANY  
BALTIMORE

---

WHEREAS, J. B. Sears, hereinafter called the Employee, has been appointed to a position in the service of California Cotton & Factorage Co., Los Angeles, Cal. hereinafter called the Employer, and

WHEREAS, said Employee has been required to furnish Bond.



NOW, THEREFORE, in consideration of a certain premium to be paid annually in advance during the term of this bond, and of the Employer's written statements relative to the Employee, his duties and accounts, it is hereby agreed that the MARYLAND CASUALTY COMPANY, a corporation of Maryland, hereinafter called the Company, will, within two (2) months after the receipt of satisfactory proofs of loss, reimburse the Employer for any loss, not exceeding Fifty Thousand Dollars (\$50,000.00), of money, securities or other personal property (including that for which the Employer may be responsible to others), which the Employer shall have sustained by reason of any act or acts of FRAUD, DISHONESTY, FORGERY, EMBEZZLEMENT, WRONGFUL ABSTRACTION or WILFUL MISAPPLICATION on the part of the Employee, while in the performance of his duties as Secretary in the service of said Employer and, occurring during the continuance of this bond.

THIS BOND is executed upon the following express conditions: which are conditions precedent to the right of the Employer to recover hereunder:

1. That the term of this bond begins at noon on the 1st day of November A. D., 1919, and ends with (a) the permanent or temporary retirement of the Employee from the service of the Employer; (b) the discovery by the Employer of loss hereunder; or (c) the cancellation of this Bond by the Employer or the Company.

2. That all statements which the Employer has furnished to the Company concerning the Employee or his duties or accounts are warranted by the Employer to be true; that the Employer has no knowledge of any act of fraud or dishonesty committed by the Employee while in the service of the Employer or elsewhere; that if the Employer become aware of the Employee committing any act of fraud or dishonesty, or of the Employee gambling or speculating or committing any disreputable, lewd or unlawful act, the Employer shall, within ten (10) days thereafter, notify the Company by registered letter, addressed to the Company at its Home Office, Baltimore, Maryland, and the Company shall not be liable for any loss subsequently incurred by the Employer through any act of the Employee unless the Company shall have consented, in writing, to continue its liability under this bond.

3. That any loss covered hereunder be discovered during the continuance of this bond or within six (6) months after its termination, and notice of such loss be sent by telegraph and by registered letter, both addressed to the Company at its Home Office, Baltimore, Maryland, within ten (10) days after the discovery; that an itemized statement of the loss shall be filed with the Company by the Employer within ninety (90) days after the date of said notice of loss; that if required by the Company, the Employer shall produce for investigation all books, vouchers, and evidence in the Employer's possession, and render every assistance (except pecuniary) capable of being rendered by the

Employer, that may aid in bringing the Employee to justice.

4. That the Employer and the Company shall share any recovery (excluding insurance and reinsurance), made by either on account of any loss, in the proportion that the amount of the loss borne by each bears to the total amount of the loss.

5. That this bond may be terminated by the Company upon fifteen (15) days' notice, in writing, to the Employer and likewise the Employer may terminate this bond by notice in writing to the Company, specifying the date of cancellation. Upon the termination of the bond and provided no loss has been reported, the Company shall refund the pro rata, unearned premium.

6. That should the Employee become guilty of any criminal offense *covered* covered by this bond, the Employer shall immediately, on being requested by the Company so to do, lay proper information before an officer or other body having authority to issue warrant for the arrest of the Employee, and verify the same as required by law, and furnish the Company every aid and assistance (not pecuniary) that can be rendered by the Employer his agents or servants, in the apprehension and prosecution of the Employee.

7. That should the Employer and the Company disagree regarding the amount of any claim made under this bond, the amount may, at the election of the Employer or the Company be determined by arbitrators; one to be selected by the Employer, one



to be selected by the Company, and a third (in the event of failure to agree upon the amount of the claim) by the two so selected; the written decision of the majority of said arbitrators shall be binding and conclusive as to the amount of such claim and the total expense of such arbitration shall be paid by the Company.

8. That no action or proceeding shall be brought to recover any claim under this bond unless begun within twelve (12) months from the time detailed statement of loss shall have been given to the Company by the Employer, unless by statute of the state in which suit is brought agreements such as in this condition contained are expressly prohibited.

SIGNED, sealed and dated this 19th day of December, A. D. 1919.

Not valid unless countersigned by an authorized official or agent of the Company.

E. E. Holly

Assistant Secretary.

(SEAL)

Jno. T. Stone

President.

Countersigned at Philadelphia, Pennsylvania this 26th day of December, A. D. 1919.

Louis J. Farley,  
attorney-in-fact."

Indorsed as follows:—"No. 134580 ENTERED LINE SHEET 5080 REGISTER R-410 MARYLAND CASUALTY COMPANY INDIVIDUAL BOND \$50,000 ON BEHALF OF J. B. Sears to California Cotton & Factorage Co. Los Angeles, Cal. Dated November 1st, 1919. For Transfers or Re-



newal, Apply to HASELTINE SMITH, FIRE, LIFE AND GENERAL INSURANCE, 326 Walnut St. Phila."

That thereafter, and on to wit: the 8th day of November, 1920, said California Cotton & Factorage Company paid to and there was accepted by said Maryland Casualty Company, defendant herein, the sum of Two hundred fifty dollars (\$250.00), being the cash premium to be paid annually in advance during the term of said bond under the provisions thereof. That by reason of the payment of said annual premium as aforesaid, said bond and all the provisions thereof were continued in full force and effect, and said bond and all the provisions thereof were in full force and effect continuously from said 26th day of December, 1919, for the term of two years thereafter.

4. That on said 26th day of December, 1919, and prior and subsequent thereto and up to and including the 3rd day of May, 1921, said J. B. Sears was then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, and as such and in his said capacity of secretary was authorized to and did act as the general manager of said California Cotton & Factorage Company, and upon its behalf and as its act and deed was authorized to and did make and enter into contracts and agreements and other instruments in writing, sign and issue checks, drafts, notes and other obligations of said California Cotton & Factorage Company, and as such secretary said J. B.

Sears, pursuant to the by-laws of said California Cotton & Factorage Company, had enjoyed and exercised complete and unrestricted power and authority to enter into any contracts or agreements and perform any and all acts and things necessary in carrying out and fulfilling the purposes and business of said California Cotton & Factorage Company.

5. That subsequent to said 26th day of December, 1919, and prior to the 3rd day of May, 1921, and at various times between said dates, the plaintiff herein, in due and regular course of business, received certain drafts drawn upon said California Cotton & Factorage Company, which said drafts, were eighty-seven in number and were in the total amount of Eighty-two thousand four hundred eighty-seven & 96/100 dollars (\$82,487.96). That attached to said eighty-seven drafts were 1476 transferable or negotiable warehouse receipts for 1476 bales of cotton; each of said warehouse receipts had been properly endorsed in blank by the party to whose order such receipt was issued, and said receipts were, and each of them was, negotiable and transferable by delivery. That immediately following the receipt of said drafts by the plaintiff herein, and within to wit: four or five days thereafter, each of said drafts was accepted in writing by said California Cotton & Factorage Company, through its said secretary, J. B. Sears, then acting within the scope of his authority and in the course of his employment. That immediately following said several acceptances, plaintiff herein remitted and paid to the person or persons pre-

senting said drafts for payment the amount or face value thereof, and upon all of said eighty-seven drafts paid and advanced to various persons presenting the same the sum of Eighty-two thousand four hundred eighty-seven & 96/100 dollars (\$82,487.96).

6. That thereafter and immediately following the acceptance of each of said drafts and the payment thereof as aforesaid, said J. B. Sears, then and there acting within the scope of his authority and within the course of his employment as secretary of said California Cotton & Factorage Company, upon behalf of, in the name of and as the act and deed of said California Cotton & Factorage Company, with the intent then and there entertained by him of fraudulently, dishonestly, wrongfully and wilfully misapplying said warehouse receipts and the proceeds thereof, applied to and secured from the plaintiff herein said warehouse receipts for fourteen hundred seventy-six (1476) bales of cotton which were attached to, and held by the plaintiff herein as collateral security for the payment of, said eighty-seven drafts and acceptances of said California Cotton & Factorage Company in the total amount of Eighty-two thousand four hundred eighty-seven & 96/100 dollars (\$82,487.96). That said J. B. Sears then and there, and as a part of and pursuant to said fraudulent and dishonest plan and scheme then and there entertained by him, delivered to and there was accepted by the plaintiff herein, in exchange or substitution for said several warehouse receipts for said 1476 bales of cotton, certain written instruments commonly known as trust receipts, eighty-



seven in number, and other than the date thereof, the numerical number attached thereto, and the number of warehouse receipts mentioned therein, were, and each of them was, of the following tenor, to wit:—

“California Cotton &  
Factorage Co.  
Cotton.

TRUST RECEIPT. No.....

. Los Angeles, California,.....

Received in trust from the The Citizens National Bank of Los Angeles Bank of Los Angeles documents, described below, the purpose being to secure delivery of the shipments and secure outbound documents therefor, which shall be returned to said bank in cancellation of this receipt.

B/L No.....No. B/C.....Mark.....

CALIFORNIA COTTON & FACTORAGE CO.

Compress or yard receipts J. B. Sears Mgr.”

.....B/C attached.

7. That thereafter and subsequent to said 26th day of December, 1919, and prior to the 3rd day of May, 1921, and during the term of said bond, and while the same was in full force and effect, said J. B. Sears then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such, within the scope of his authority and in the course of his employment, without the knowledge of said California Cotton & Factorage Company, or any of its officers,



or agents, other than said J. B. Sears, fraudulently, dishonestly, wrongfully and wilfully embezzled and misapplied said warehouse receipts for 1091 bales of cotton, together with the proceeds thereof. That said receipts were a part or portion of the warehouse receipts representing a total of 1476 bales of cotton, which receipts said J. B. Sears had obtained from the plaintiff herein as hereinbefore alleged.

That said 1476 bales of cotton, for which said J. B. Sears had obtained said warehouse receipts, from the plaintiff herein, as aforesaid, at the time said receipts were so secured by said J. B. Sears, were of the reasonable value of Eighty-two thousand four hundred and eighty-seven & 96/100 dollars (\$82,487.96). That said 1091 bales of cotton, the warehouse receipts for which, and the proceeds of the sale and disposition thereof, said J. B. Sears had fraudulently, dishonestly, wrongfully and wilfully embezzled and misapplied, as herein alleged, at the time said receipts and the proceeds thereof were fraudulently, dishonestly and wilfully embezzled and misapplied, were of the reasonable value of Sixty thousand six hundred and twenty-eight & 72/100 dollars (\$60,628.72). Upon information and belief, plaintiff alleges that there was received by said California Cotton & Factorage Company, and thereafter fraudulently, dishonestly, wrongfully and wilfully embezzled and misapplied by said J. B. Sears, as its secretary, through the fraudulent and dishonest embezzlement and disposition of said warehouse receipts for said 1091 bales of cotton, and the proceeds thereof, the sum of Sixty thousand six

hundred twenty-eight & 72/100 dollars (\$60,628.72), which amount was thereafter, during the term of said bond, fraudulently and dishonestly embezzled and wilfully misapplied by said J. B. Sears, acting in his capacity as secretary of said California Cotton & Factorage Company.

8. That thereafter and subsequent to said 26th day of December, 1919, and prior to the 3rd day of May, 1921, and during the term of said bond and while the same was in full force and effect, the said J. B. Sears, then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such, within the scope of his authority and in the course of his employment, having obtained said 1476 warehouse receipts for said fourteen hundred and seventy-six (1476) bales of cotton and substituted therefor the seventy-eight trust receipts of said California Cotton & Factorage Company, all as hereinbefore alleged, pursuant to a fraudulent and dishonest plan and scheme then and there entertained by him, fraudulently, dishonestly, wrongfully, wilfully and deceitfully, with the intent then and there by him entertained of fraudulently, dishonestly, wrongfully and wilfully misapplying and embezzling the proceeds realized from the sale and disposition of the cotton held in trust by said California Cotton & Factorage Company, under the trust receipts delivered to and accepted by the plaintiff herein, as hereinbefore alleged, misrepresented to said California Cotton & Factorage Company, its officers and board of directors, that the moneys realized from the sale and disposition of said

cotton held in trust for said Citizens National Bank as aforesaid, were and the same constituted the profits of carrying on the affairs of said California Cotton & Factorage Company; and thereafter, pursuant to said fraudulent and dishonest plan or scheme, then and there entertained by said J. B. Sears, and pursuant to a fraudulent and dishonest intent then and there entertained by him to deceive said California Cotton & Factorage Company, and its officers and agents, and in wilful violation of the terms of said trust receipts, held by said Citizens National Bank as hereinbefore mentioned, and in wilful violation of his duties as secretary of said California Cotton & Factorage Company, fraudulently, dishonestly, wrongfully and wilfully misapplied said warehouse receipts and the proceeds and moneys realized from the sale or other disposition of said warehouse receipts and the cotton held thereunder, to the payment and satisfaction of divers and sundry claims for merchandise and supplies furnished and labor and services rendered to, and other claims and demands against, said California Cotton & Factorage Company, but not including the whole, or any part, of the claim of the plaintiff herein against said California Cotton & Factorage Company, upon the drafts, or any one thereof, accepted by said California Cotton & Factorage Company and held by said plaintiff, and to which were attached, as collateral security, the warehouse receipts for which there had been substituted by said J. B. Sears the trust receipts of said California Cotton & Factorage Company, as hereinbefore alleged.



9. That due to, growing out of, and because of, the fraud, dishonesty, wrongful and wilful misapplication of the warehouse receipts, the cotton held thereunder, and the moneys and proceeds realized from the sale or disposition thereof by said J. B. Sears, as secretary of said California Cotton & Factorage Company, as hereinbefore alleged, said California Cotton & Factorage Company has sustained a loss in the amount of Sixty thousand six hundred twenty-eight & 72/100 dollars (\$60,628.72), and has become and is responsible to the plaintiff herein for said amount.

10. That thereafter, and following said fraudulent, dishonest, wrongful and wilful misapplication by said J. B. Sears of the moneys, securities and personal property of said California Cotton & Factorage Company, as herein alleged, said California Cotton & Factorage Company, pursuant to the terms of said bond, and immediately upon the discovery by it of said loss sustained and said responsibility incurred, as hereinbefore alleged, and within ten days after such discovery, notified said Maryland Casualty Company at its home office, Baltimore, Maryland, by telegraph and by registered letter, of such loss sustained and of such responsibility incurred, and within ninety days after the date of said notice of loss filed with said Maryland Casualty Company at its home office at Baltimore, Maryland, an itemized statement of said loss so sustained and said liability so incurred, and thereafter, upon the request of said Maryland Casualty



Company, produced for investigation, and there were investigated by said Maryland Casualty Company, all books, vouchers and evidence in the possession of said California Cotton & Factorage Company. That said J. B. Sears is now deceased, having committed suicide on the 3rd day of May, 1921.

That notwithstanding the service of said notices upon the defendant herein, by said California Cotton & Factorage Company, said defendant has failed and refused, and still fails and refuses to reimburse said California Cotton & Factorage Company for the loss it has sustained, and the responsibility to others it has incurred under the terms of said bond by reason of the fraud, dishonesty, embezzlement, wrongful abstraction and wilful misapplication on the part of said J. B. Sears, while in the performance of his duties as secretary of said California Cotton & Factorage Company, as hereinbefore alleged.

11. That heretofore, and on to wit: the 9th day of May, 1922, the plaintiff herein obtained a judgment against said California Cotton & Factorage Company in the amount of Ninety thousand two hundred eighty one & 01/100 Dollars, in the superior court of the state of California, in and for the county of Los Angeles, said judgment being entered in book 535, at page 30, of the records of judgments of said Los Angeles County, state of California; that said judgment was had on said drafts, accepted by said California Cotton & Factorage Company, as hereinbefore alleged, and said trust receipts substituted by said J. B. Sears for said warehouse receipts.

12. That heretofore and on to wit: the 1st day of September, 1921, California Cotton & Factorage Company, by an instrument in writing, assigned, transferred and set over to the plaintiff all its right, title or interest in and to said bond hereinbefore described, and in and to all moneys due or to become due, including all claims, demands, causes of action or choses in action in every clause, article or thing in said bond contained.

PLAINTIFF, FOR A FURTHER, SEPARATE AND SECOND CAUSE OF ACTION AGAINST THE SAID DEFENDANT, ALLEGES:—

1. That paragraphs 1, 2, 3, 4, 10 and 12, of the first cause of action, are hereby referred to, incorporated herein, and made a part of this second cause of action with the same force and effect as if set out herein at length.

2. That subsequent to said 26th day of December, 1919, and prior to the 3rd day of May, 1921, and at various times between said dates, and during the term of said bond, and while the same was in full force and effect, said J. B. Sears then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such within the scope of his authority and in the course of his employment, without the knowledge of said California Cotton & Factorage Company, or any of its officers or agents, other than said J. B. Sears, fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and wilfully misapplied the money and funds of said California

Cotton & Factorage Company in the amount of five thousand five hundred and three & 88/100 dollars (\$5,503.88) to his own uses and purposes, and in satisfaction of his personal obligations. That said moneys or funds in the amount of five thousand five hundred and three & 88/100 dollars (\$5,503.88) were, by said J. B. Sears, withdrawn from the moneys and funds of the California Cotton & Factorage Company in the possession of said J. B. Sears, or on deposit with the Citizens National Bank of Los Angeles, plaintiff herein.

3. That due to, growing out of, and because of, the fraud, dishonesty, embezzlement, wrongful abstraction and wilful misapplication on the part of said J. B. Sears, of the moneys and funds of said California Cotton & Factorage Company, as hereinbefore alleged, said California Cotton & Factorage Company has sustained a loss in the amount of Five thousand five hundred and three & 88/100 dollars (\$5,503.88).

WHEREFORE, plaintiff prays judgment against defendant for the sum of Fifty thousand dollars (\$50,000.00) with interest thereon at seven per cent per annum from the third day of May, 1921, and for costs of suit.

Hunsaker, Britt & Cosgrove

Attorneys for plaintiff.

STATE OF CALIFORNIA, County of Los Angeles—ss.

A. J. WATERS, being first duly sworn, deposes and says: That I am President of The Citizens National Bank of Los Angeles, plaintiff herein, named in the



foregoing complaint; that I have read said complaint and know the contents thereof, and that the same is true of my own knowledge, except as to those matters which are therein stated upon information or belief, and as to those matters, I believe it to be true.

A. J. WATERS

Subscribed and sworn to before me this 6th day of May, 1922.

(SEAL)

C. E. FISH

Notary Public in and for said County of Los Angeles.

[Endorsed]: No. 106090 Dept..... SUPERIOR COURT OF THE STATE OF CALIFORNIA In and for the County of Los Angeles THE CITIZENS NATIONAL BANK, OF LOS ANGELES, Plaintiff vs. MARYLAND CASUALTY COMPANY, Defendant COMPLAINT. INSURANCE POLICY. FILED 1922 MAY 11 P M 3 29 L. E. LAMPTON, County Clerk By Roy Goff Deputy.

IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

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THE CITIZENS NATIONAL )	
BANK, OF LOS ANGELES, )	
Plaintiff, )	No. 1124—Civil.
—vs— )	DEMURRER TO
MARYLAND CASUALTY )	COMPLAINT AS
COMPANY, a Corporation, )	AMENDED.
Defendant. )	

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Now comes the defendant and demurs to the complaint as amended, to-wit, the first cause of action:



## I.

Upon the ground that said complaint, as amended, does not state facts sufficient to constitute a cause of action in favor of the plaintiff and against the defendant.

## II.

(a) Defendant demurs specially: upon the ground that said complaint, as amended, is ambiguous in that it cannot be ascertained or determined as a matter of fact how, or in what way or manner the said J. B. Sears "fraudulently and dishonestly converted, misappropriated, embezzled and wilfully misapplied the moneys and funds placed to the credit of said California Cotton & Factorage Company" by his alleged dealing and speculating in cotton. (Paragraph 8, page 8.)

(b) That said complaint, as amended, is ambiguous in that it cannot be ascertained what claims and demands were incurred or paid by said J. B. Sears in his alleged dealing and speculating in cotton. (Page 8, Paragraph 8.) Nor can it be ascertained whether all of the money alleged to have been used by said J. B. Sears for the purpose of dealing and speculating in cotton was with the permission of the California Cotton & Factorage Company, its directors and officers. (Paragraph 8, pages 8 and 9).

## III.

That said complaint, as amended, is unintelligible in each and all of the particulars as set forth in Paragraph II, sections a and b.

IV.

That said complaint, as amended, is uncertain in each and all of the particulars as set forth in Paragraph II, sections a and b.

Bicksler, Smith & Parke

Attorneys for Defendant.

[Endorsed]: (ORIGINAL) No. 1124—Civil In The UNITED STATES DISTRICT COURT In and for the Southern District of California, Southern Division. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff -vs- MARYLAND CASUALTY COMPANY, a Corporation, Defendant. DEMURRER TO COMPLAINT AS AMENDED. FILED AUG 31 1922 CHAS. N. WILLIAMS, Clerk By W. J. Tufts Received copy of the within Demurrer this 31st day of August 1922 Hunsaker, Britt & Cosgrove Attorney for Plaintiff. BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant.

IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN DIS-  
TRICT OF CALIFORNIA,  
SOUTHERN DIVISION.

- - - - -		
THE CITIZENS NATIONAL )		
BANK OF LOS ANGELES, )		
Plaintiff, )	NOTICE OF	
- vs - )	MOTION	
)	TO STRIKE.	
MARYLAND CASUALTY )		
COMPANY, a Corporation, )		
Defendant. )		
- - - - -		

To The Citizens National Bank of Los Angeles,  
Plaintiff:

To Messrs. Hunsaker, Britt & Cosgrove, Attorneys  
for Plaintiff:

You and each of you will take notice that on Mon-  
day, June 26, 1922, in the above entitled Court, de-  
fendant will move to strike from the complaint herein  
the following:

(1) All of Paragraph 11 of the first cause of ac-  
tion, reading as follows:

"That theretofore, and on to wit: The 9th day  
of May, 1922, the plaintiff herein obtained a  
judgment against said California Cotton & Fac-  
torage Company in the amount of Ninety Thou-  
sand Two Hundred Eighty One & 01/100 Dol-  
lars, in the Superior Court of the State of Cali-  
fornia, in and for the County of Los Angeles,  
said judgment being entered in Book 535, at page  
30, of the records of judgments of said Los An-

geles County, State of California; that said judgment was had on said drafts, accepted by said California Cotton & Factorage Company, as hereinbefore alleged, and said trust receipts substituted by said J. B. Sears for said warehouse receipts."

(2) All of Paragraph 12 of the first cause of action, reading as follows:

"That heretofore and on to wit: The 1st day of September, 1921, California Cotton & Factorage Company, by an instrument in writing, assigned, transferred and set over to the plaintiff all its right, title or interest in and to said bond hereinbefore described, and in and to all moneys due or to become due including all claims, demands, causes of action or choses in action in every clause, article or thing in said bond contained."

(3) That portion of Paragraph I of the second alleged cause of action, which incorporates Paragraph 12 of the first cause of action.

Said motion will be based upon the grounds that the parts sought to be stricken out are surplusage, redundant and immaterial; that only parties to a judgment are bound thereby; and that an assignee in an alleged claim upon the bond herein cannot sue thereon; and upon the record, files and proceedings herein.

Dated—June 14th, 1922.

Bicksler, Smith & Parke

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Attorneys for Defendant.



## POINTS AND AUTHORITIES:

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Judgment binding only on parties and successors in interest.

Silva v. Hawkins, 152 Cal. 138.

Merriam v Saalfeld, 190 Fed. 927.

Assignee cannot sue on said bond.

Childs on Suretyship, Section 135.

Flynn v North America Life Ins. Co., 115 Mass. 449.

[Endorsed]: (ORIGINAL) No 1124 Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California, Southern Division. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, - -vs - MARYLAND CASUALTY COMPANY, a Corporation, defendant. NOTICE OF MOTION TO STRIKE. FILED JUN 17 1922 CHAS. N. WILLIAMS, Clerk By Edmund L. Smith Deputy Clerk Received copy of the within Notice this 16th day of June, 1922 Hunsaker, Britt & Cosgrove Attorney for Plaintiff. BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant.

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At a stated term, towit: the July, A. D., 1922 Term of the District Court of the United States of America, within and for the Southern Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, on Mon-

day, the thirty-first day of July, in the year of our  
Lord, one thousand nine hundred and twenty-two;  
Present:

The Honorable Benjamin F. Bledsoe, District Judge.

The Citizens National Bank	)	
of Los Angeles,	)	
	)	
Plaintiff,	)	
vs.	)	No. 1124 Civil.
	)	
Maryland Casualty Company,	)	
Defendant.	)	

This cause coming on at this time for (1) hearing on Demurrer and (2) hearing on motion to strike and at the hour of 1:30 o'clock P. M. Attorney Smith of Messrs. Bicksler, Smith & Parke appearing on behalf of the defendant, having argued in support of the motion to strike and the demurrer, and at the hour of 1:55 o'clock P. M. attorney Cosgrove of Messrs. Hunsaker, Britt & Cosgrove, appearing on behalf of the plaintiff herein, having argued in opposition to motion to strike and the demurrer, it is by the court ordered at the hour of two o'clock P. M. that this cause be continued to the hour of 2:35 o'clock P. M. and now at the hour of 2:35 o'clock P. M. attorney Cosgrove having resumed his argument in opposition to the motion to strike and the demurrer, it is by the court ordered, at the hour of 3:50 o'clock P. M. that the Demurrer be sustained as to the first cause of action; denied as to the second cause of action and that the motion to strike be denied; and it is further ordered by the court that plaintiff herein have thirty days to

amend first cause of action and that defendant have thirty (30) days to answer the plaintiff's second cause of action.

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UNITED STATES DISTRICT COURT IN AND  
FOR THE SOUTHERN DISTRICT OF CALI-  
FORNIA, SOUTHERN DIVISION.

THE CITIZENS NATIONAL )  
BANK, ) #1124  
Plaintiff, )  
vs. ) AMENDMENT TO  
MARYLAND CASUALTY ) COMPLAINT—  
COMPANY, a corporation, ) FIRST CAUSE OF  
Defendant. ) ACTION.

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Comes now The Citizens National Bank of Los Angeles, plaintiff herein, and with leave of court first had and obtained, files this its amendment to its first cause of action as set forth in its complaint on file herein and amends said first cause of action as follows:—

1. Amends paragraph 5 of said first cause of action so that the same shall read as follows:—

5. That subsequent to said 26th day of December, 1919, and prior to said 3rd day of May, 1921, and during the term of said bond, and beginning more particularly on or about the 19th day of November, 1920, and at various times and at irregular intervals thereafter up to and including on or about the 25th day of April, 1921, the plaintiff herein, in due and regular course of business, received eighty-seven drafts drawn

upon said California Cotton & Factorage Company, in the total amount of \$82,487.96. That attached to each of said eighty-seven drafts were one or more warehouse receipts, each receipt covering one bale of cotton, and that there were attached to said eighty-seven drafts so received a total of 1476 warehouse receipts for 1476 bales of cotton; that each warehouse receipt had been, at the time of its receipt by the plaintiff herein, endorsed in blank by the party to whose order such receipt had been issued, and said receipts were, and each of them was, negotiable and transferable by delivery. That immediately following the receipt of each of said drafts by the plaintiff herein, and within, to wit, four or five days thereafter, each of said drafts was accepted in writing by said California Cotton & Factorage Company, by its said Secretary, J. B. Sears, then acting within the scope of his authority and the course of his employment. That immediately following said several acceptances of said California Cotton & Factorage Company, as herein alleged, and relying entirely thereon and for no other reason, plaintiff herein remitted and paid to the person or persons presenting said drafts for acceptance and payment, the amount or face value thereof, and thereafter carried upon its books and accounts as bills receivable all such drafts and acceptances so received and paid and all warehouses receipts attached thereto were held by plaintiff as collateral security for the payment by said California Cotton & Factorage Company of said drafts and acceptances. That the total face value of said 87 drafts was in the sum of



\$82,487.96, which sum the plaintiff herein paid and advanced, as herein alleged, to the various persons presenting the same.

2. Amends paragraph 6 of said first cause of action so that the same shall read as follows:—

6. That at various times and at irregular intervals between said 19th day of November, 1920, and said 25th day of April, 1921, and in most instances immediately following the acceptance of each of said drafts and the payment thereof as hereinbefore alleged, said J. B. Sears, then and there acting within the scope of his authority and the course of his employment as Secretary of said California Cotton & Factorage Company, upon behalf, in the name and as the act and deed of said California Cotton & Factorage Company, with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating, embezzling and wilfully misapplying said warehouse receipts, the cotton represented thereby and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained of thereby causing a loss to said California Cotton & Factorage Company of money, securities and personal property for which it would be and has become responsible to the plaintiff herein, said J. B. Sears applied to and secured from the plaintiff the warehouse receipts then in its possession, held as collateral security for the payment of said drafts and acceptances and obtained by it in the manner herein alleged; that at said time and as part of the same transaction, in acknowledgment of the de-

livery to him of said warehouse receipts, said J. B. Sears executed and delivered to the plaintiff certain written instruments then and there designated as trust receipts; that during all of the time hereinbefore mentioned, said J. B. Sears executed and delivered to the plaintiff 87 of said trust receipts, which trust receipts, other than the number and date thereof, and the amount of warehouse receipts mentioned therein, were of the following tenor and effect:—

TRUST RECEIPT.

“California Cotton & No.....  
Factorage Co.  
Cotton.

Los Angeles, California,—————

Received in trust from The Citizens National Bank of Los Angeles Bank of Los Angeles documents, described below, the purpose being to secure delivery of the shipments and secure outbound documents therefor, which shall be returned to said bank in cancellation of this receipt.

B/L No.—— No. B/C—— Mark——

CALIFORNIA COTTON & FACTORAGE CO.  
Compress or yard receipts. J. B. Sears, Mgr.”  
———B/C attached.

That said J. B. Sears, at the time of receiving said warehouse receipts and executing and delivering said trust receipts, represented to the plaintiff, its officers and agents, that in order to make and complete sales of the cotton covered by said warehouse receipts it would be necessary to surrender said warehouse receipts to the persons, firms, or corporations issuing the

same, and obtain possession of and deliver said cotton to the common carriers of freight over which shipments of said cotton would be made to the purchasers thereof, receiving in exchange therefor the bills of lading of the said common carriers; that upon any such exchange being made he, the said J. B. Sears, would immediately thereafter return said bills of lading to the plaintiff herein, and at such time take up the trust receipt or trust receipts given by him to the plaintiff at the time and in acknowledgment of the delivery to him of warehouse receipts covering cotton sold as aforesaid.

That in said manner and pursuant to said fraudulent and dishonest plan and scheme, said J. B. Sears at various times and irregular intervals procured from the plaintiff herein between the said 19th day of November, 1919, and said 25th day of April, 1921, 1476 warehouse receipts for 1476 bales of cotton, and issued and delivered to the plaintiff in acknowledgment thereof 87 of said trust receipts.

3. Amends paragraph 7 of said first cause of action so that the same shall read as follows:—

7. That subsequent to said 19th day of November, 1920, and prior to said 3rd day of May, 1921, and at various times and irregular intervals between said dates, said J. B. Sears, then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such, within the scope of his authority and the course of his employment, without the knowledge of said California Cotton & Factorage Company, or any



of its officers, or agents, other than said J. B. Sears, pursuant to said fraudulent and dishonest plan and scheme by him entertained as hereinbefore alleged, fraudulently and dishonestly converted, misappropriated, embezzled and wilfully misapplied 1091 of said 1476 warehouse receipts and 1091 bales of cotton represented thereby in the manner following, to-wit, that is to say, said J. B. Sears, having obtained said warehouse receipts in the manner and for the purpose herein alleged, sold said cotton covered by said receipts to various and divers purchasers of cotton throughout the United States; that thereupon said J. B. Sears surrendered said warehouse receipts to the persons, firms and corporations issuing the same, secured possession of and delivered said cotton to common carriers of freight at various points in the states of California and Arizona for shipment and delivery to the purchasers thereof and received from said common carriers bills of lading for said shipments of cotton. That said J. B. Sears immediately thereafter, in violation of his duties as secretary of California Cotton & Factorage Company, and in wilful violation of his promises and representations to the plaintiff, and in violation of the terms of said trust receipts, delivered by him to the plaintiff, all as herein alleged, but pursuant to said fraudulent and dishonest plan and scheme alleged herein, attached said bills of lading to sight drafts prepared by him and drawn upon the purchasers of said cotton, by the California Cotton & Factorage Company in favor of the Citizens National Bank of Los Angeles, and thereupon presented said



sight drafts with bill of lading attached for approval, acceptance and the immediate issuance of credit thereon, to an officer of said bank, other than the officer or officers from whom said J. B. Sears had obtained said warehouse receipts, and to whom he had delivered said trust receipts, and represented to said officer or officers to whom said sight drafts and bills of lading were presented that the cotton covered by said sight drafts and bills of lading was cotton belonging to said California Cotton & Factorage Company over which it had unrestricted right of disposal, and failed to disclose to said officer or officers the fact that said bank then held trust receipts of said California Cotton & Factorage Company, given by said J. B. Sears under the circumstances and for the purposes as hereinbefore alleged, covering the cotton described in said bills of lading attached to said sight drafts. That thereupon said J. B. Sears, having first secured the approval of said officer of said bank, deposited said sight drafts with bills of lading attached with said officers of said plaintiff bank and received at that time from said officers and from said bank credit upon the account of said California Cotton & Factorage Company for the amount of said sight draft. That at the same time said J. B. Sears presented to a teller of said bank the bank pass book of said California Cotton & Factorage Company and there was entered therein by said teller as a deposit in said bank to the credit of the account of said California Cotton & Factorage Company an amount equal to the amount of said sight draft; that said J. B. Sears immediately thereafter, pursuant to

said fraudulent scheme hereinbefore mentioned, falsified the books and accounts of said California Cotton & Factorage Company by entering, or causing to be entered therein, the various amounts of money received from the various sales of cotton made and carried out, as alleged herein, and the various amounts shown as having been deposited and the various credits entered as aforesaid upon the bank pass book of said California Cotton & Factorage Company, as moneys and funds belonging wholly and entirely, without claim or restriction of any kind, to said California Cotton & Factorage Company; and then and there wilfully failed to enter in said books of said California Cotton & Factorage Company any entry or memorandum showing the nature of the said transactions, as alleged herein, or the manner in which said warehouse receipts had been secured, or that any trust receipts had been issued, as herein alleged, or that said moneys and credits entered in said bank pass book were received, as alleged herein, and wilfully failed to make, or cause to be made, any other entry or memorandum indicating that said funds or moneys were charged with any trust or were in any manner money and funds other than the absolute and unencumbered property and funds of said California Cotton & Factorage Company.

That during and following the transactions of said J. B. Sears, as herein alleged, said J. B. Sears frequently represented to said California Cotton & Factorage Company, its officers and directors, that said various sums of money and said credits entered upon

said bank pass book and books of account of said California Cotton & Factorage Company, as aforesaid, were the funds and moneys of said California Cotton & Factorage Company made or accumulated by said J. B. Sears in the conduct of the affairs of said California Cotton & Factorage Company; and, though well knowing of the disposition and sale of said warehouse receipts and cotton as herein alleged, said J. B. Sears, upon inquiry made of him, represented to the plaintiff and its officers at various and divers times between said dates that the said California Cotton & Factorage Company still retained, and that he, the said J. B. Sears, as secretary of said California Cotton & Factorage Company, still had in his custody in the vaults and files of said California Cotton & Factorage Company, all and every the various warehouse receipts surrendered to him by said plaintiff, as herein alleged. That the California Cotton & Factorage Company and the Citizens National Bank of Los Angeles, and the directors and officers of each of said corporations, believed, acted upon and were deceived by said dishonest and fraudulent representations and statements of said J. B. Sears.

That said 1091 bales of cotton disposed of by said J. B. Sears, as herein alleged, were, at the time of such sale and disposition, of the reasonable value of \$60,628.72, which amount plaintiff, upon information and belief, alleges was credited to the account of said California Cotton & Factorage Company in the manner herein alleged.

4. Amends paragraph 8 of said first cause of action so that the same shall read as follows:—



8. That subsequent to said 19th day of November, 1920, and prior to said 3rd day of May, 1921, and at various and irregular intervals between said dates, pursuant to said fraudulent and dishonest plan and scheme hereinbefore alleged, and contemporaneous with the several fraudulent and dishonest conversions, misappropriations, embezzlements and wilful misapplications of said warehouse receipts, the cotton represented thereby, the bills of lading for the same, and the moneys and credits realized therefrom, and the false and fraudulent representations made and deceit practiced by said J. B. Sears upon the California Cotton & Factorage Company and the plaintiff, and their, and each of their, officers and agents, all as herein alleged, said J. B. Sears, continuing to act within the scope of his authority and the course of his employment as secretary of said California Cotton & Factorage Company, fraudulently and dishonestly converted, misappropriated, embezzled and wilfully misapplied the moneys and funds placed to the credit of said California Cotton & Factorage Company following the various dishonest and fraudulent sales of cotton and dispositions of said warehouse receipts and bills of lading, as herein alleged, by using said moneys and funds for the purpose of dealing and speculating in cotton and conducting such dealings and speculations at a loss and paying said losses out of said moneys and funds and in the payment of claims and demands incurred by said J. B. Sears, in said dealings and speculations in cotton.



That no part of said sum of \$60,628.72 was used by said J. B. Sears or by any other person in the payment or satisfaction, either in whole or in part, of any one or more of said 87 drafts and acceptances of the California Cotton & Factorage Company, held by the plaintiff, as herein alleged.

That relying entirely upon said false and fraudulent representations of said J. B. Sears, and said deceits by him practiced upon it and them, said California Cotton & Factorage Company, its directors and officers continued the business of said California Cotton & Factorage Company and allowed and permitted said J. B. Sears, subsequent to on or about said 19th day of November, 1920, to continue to act as the secretary of said company and to continue to perform the acts and things necessary in carrying out the business of said California Cotton & Factorage Company, and to continue to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith. That said California Cotton & Factorage Company, its directors and officers, would not have continued the business of said California Cotton & Factorage Company subsequent to on or about the 19th day of November, 1920, neither would they have allowed said J. B. Sears to continue to act as secretary of said California Cotton & Factorage Company after on or about said date, neither would they subsequent to said date have allowed said J. B. Sears to conduct any dealings or speculations in cotton nor incur any indebtedness nor contract any financial obligations upon its behalf, had it or any of its direc-

tors or officers, other than said J. B. Sears, known of the frauds, deceits, dishonesties, wrongful conversions, embezzlements, misappropriations and wilful misapplications, or any of them, being practiced upon them, and upon said Citizens National Bank of Los Angeles by said J. B. Sears, as herein alleged.

5. Amends paragraph 9 of said first cause of action so that the same shall read as follows:—

9. That due to, growing out of, and because of, the fraud, dishonesty, embezzlement, wrongful abstraction and wilful misapplication of said warehouse receipts, the cotton held thereunder, said bills of lading and the moneys, proceeds and credits realized from the sale and disposition thereof by said J. B. Sears as secretary of said California Cotton & Factorage Company in the manner herein alleged, said California Cotton & Factorage Company has sustained a loss, and has become, and is, responsible to the plaintiff herein in the amount of \$60,628.72.

WHEREFORE, plaintiff prays judgment against defendant for the sum of Fifty thousand dollars (\$50,000.00), with interest thereon at 7% per annum from the third day of May, 1921, and for costs of suit.

Hunsaker, Britt &amp; Cosgrove,

Attorneys for Plaintiff.

STATE OF CALIFORNIA, )  
County of Los Angeles. ) ss.

A. J. WATERS, being first duly sworn, deposes and says:

That I am President of The Citizens National Bank, of Los Angeles, plaintiff herein, named in the foregoing Amendment to Complaint—First Cause of Action; that I have read said Amendment to Complaint—First Cause of Action, and know the contents thereof, and that the same is true of my own knowledge, except as to those matters which are therein stated upon information or belief, and as to those matters, I believe it to be true.

A. J. Waters

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Subscribed and sworn to before me this 23rd day of August, 1922.

(Seal)

C. C. Wall

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Notary Public in and for said  
County of Los Angeles.

[Endorsed]: ORIGINAL No. 1124 IN THE United States District Court Southern District of California Southern Division THE CITIZENS NATIONAL BANK, Plaintiff, vs. MARYLAND CASUALTY COMPANY, a corporation, Defendant. AMENDMENT TO COMPLAINT—FIRST CAUSE OF ACTION. Receipt of a copy of the within is hereby admitted this 24 day of August 1922. Bicksler, Smith & Parke, Attorney.. for ..... FILED AUG 25 1922 CHAS. N. WILLIAMS Clerk By W. J. Tufts Deputy Clerk HUNSAKER, BRITT & COSGROVE 1132 1143 Title Insurance Building Fifth and Spring Streets Los Angeles, Cal. Attorneys for Plaintiff.

IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN DIS-  
TRICT OF CALIFORNIA,  
SOUTHERN DIVISION.

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THE CITIZENS NATIONAL )  
BANK OF LOS ANGELES, )  
Plaintiff, ) DEMURRER  
-vs- ) of  
 ) Defendant.  
MARYLAND CASUALTY )  
COMPANY, a Corporation, )  
Defendant. )  
-----

Now comes defendant and demurs to the first alleged cause of action in the complaint herein, upon the following grounds:

I.

That said alleged first cause of action of said complaint does not state facts sufficient to constitute a cause of action in favor of the plaintiff and against the defendant.

II.

That there is a defect of parties in that the California Cotton & Factorage Company should be joined as plaintiff.

III.

(a) That said first alleged cause of action in said complaint is ambiguous in that it cannot be ascertained and determined, as a matter of fact, how, or in what way or manner said J. B. Sears "fraudulently, dishonestly, wrongfully or wilfully misapplied said warehouse receipts or the proceeds thereof". (Paragraph 6 of the first cause of action of said complaint.)



(b) That said first alleged cause of action of said complaint is ambiguous in that it cannot be ascertained and determined, as a matter of fact, how, or in what way or manner said J. B. Sears "fraudulently, dishonestly, wrongfully, or wilfully embezzled or misapplied said warehouse receipts" for said cotton, and/or the proceeds thereof. (Paragraph 7 of the first alleged cause of action of said complaint.)

(c) That said first alleged cause of action of said complaint is ambiguous in that it cannot be ascertained and determined, as a matter of fact, how, or in what way or manner "because of said fraud, dishonesty, wrongful and wilful misapplication of said warehouse receipts, the cotton held thereunder, and the moneys and proceeds realized from the sale or disposition thereof by said J. B. Sears, as secretary of said California Cotton & Factorage Company, said California Cotton & Factorage Company has sustained a loss in the amount of \$60,628.72", or any other sum of money. (Paragraph 9 of the first alleged cause of action of said complaint.)

(d) That said first alleged cause of action of said complaint is ambiguous in that it cannot be ascertained and determined, as a matter of fact, how, or in what way or manner the California Cotton & Factorage Company has any "responsibility to others, incurred under the terms of said bond by reason of the fraud, dishonesty, embezzlement, wrongful abstraction and wilful misapplication on the part of said J. B. Sears." (Paragraph 10 of the first alleged cause of action of said complaint.)

IV.

That said first alleged cause of action in said complaint is unintelligible in each and all of the particulars as set forth in Paragraph III, Sections a, b, c and d, hereof.

V.

That said first alleged cause of action in said complaint is uncertain in each and all of the particulars as set forth in Paragraph III, Sections a, b, c and d hereof.

Defendant demurs to the further, separate and second alleged cause of action in the complaint herein, upon the following grounds:

I.

That said alleged second cause of action of said complaint does not state facts sufficient to constitute a cause of action in favor of the plaintiff and against the defendant.

II.

(a) That said second alleged cause of action in said complaint is ambiguous in that it cannot be ascertained and determined, as a matter of fact, how, or in what way or manner said "J. B. Sears, fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and wilfully misapplied the money and funds of said California Cotton & Factorage Company \* \* to his own uses and purposes, or in satisfaction of his personal obligations". (Paragraph 2 of the second cause of action of said complaint.)

(b) That said second alleged cause of action in said complaint is ambiguous in that it cannot be ascer-

tained and determined, as a matter of fact, how, or in what way or manner said "California Cotton & Fac-torage Company has sustained a loss in the amount of \$5,503.88", or in any other amount of money. (Para-graph 3 of the second alleged cause of action of said complaint.)

### III.

That said second alleged cause of action in said complaint is unintelligible in each and all of the particulars as set forth in Paragraph II, Sections a and b, hereof.

### IV.

That said second alleged cause of action in said complaint is uncertain in each and all of the particulars as set forth in Paragraph II, Sections a and b, hereof.

Bicksler, Smith & Parke

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Attorneys for Defendant.

### POINTS AND AUTHORITIES:

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Complaint insufficient.

U. S. Judicial Code,

Section 255, Article 5. (U. S. R. S. 914)

Pleadings and proceedings thereunder governed by State Law.

Foster's Federal Practice, Section 454.

Assignee cannot sue upon cause of action stated herein.

Childs on Suretyship, Section 135.

And cases cited.

Flynn v. North America Life Ins. Co.

115 Mass. 449.

9 Corpus Juris, page 53:

"A bond conditioned for the performance of a personal act or service is generally held not assignable within the meaning of the statutes".

THERE WAS NEITHER WRONGFUL AB-  
STRACTION NOR WILFUL MISAPPLICATION  
OF FUNDS.

Guarantee Company v. Mechanics Savings  
Bank, 100 Fed. 559;

Rosenlee v. American Surety Company,  
91 N. J. L. 591.

Jackson v. First National Bank,  
42 N. J. L. 177.

Walsh v. U. S., 192 Fed. 561.

Monongahela Coal Co. v. Fidelity &  
Deposit Co., 94 Fed. 732.

Dixie Fire Ins. Co. v. Nelson,  
128 Tenn. 71.

Milwaukee Theater Co. v. Fidelity &  
Deposit Co., 92 Wis. 412.

Kansas Flour Co. v. American Surety Co.,  
98 Kas. 618.

Clarke v. Fidelity & Deposit Company,  
73 Wash. 65.



Complaint is uncertain—pleading conclusions and not facts.

Evans v. U. S., 153 U. S. 588.

U. S. v. Britton, 107 U. S. 655.

Fox v. Hale, 108 Cal. 370, 426.

Water Works v. San Francisco,  
82 Cal. 321.

[Endorsed]: (ORIGINAL) No 1124 Civil In the UNITED STATES DISTRICT COURT IN and for the Southern District of California, Southern Division. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, - vs - MARYLAND CASUALTY COMPANY, a Corporation, Defendant. DEMURRER OF Defendant. FILED JUN 17 1922 CHAS. N. WILLIAMS, Clerk Edmund L. Smith Deputy Clerk Received copy of the within Demurrer this 16th day of June 1922 Hunsaker, Britt & Cosgrove. Attorney for plaintiff BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant.

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At a stated term, to wit: the July Term, A. D., 1922, of the District Court of the United States of America, within and for the Southern Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, on Monday, the sixth day of November, in the year of our Lord, one thousand nine hundred and twenty-two;

Present:

The Honorable Benjamin F. Bledsoe, District Judge.

Citizens National Bank of Los Angeles,	)	
	)	
Plaintiff	)	
vs.	)	No. 1124 Civil, S.D.
	)	
Maryland Casualty Company,	)	
Inc. et al.	)	
Defendants.	)	

This cause coming on at this time for hearing on demurrer to first cause of action as amended; Attorney Cosgrove of Messrs. Hunsaker Britt & Cosgrove appearing as counsel for the plaintiff and Attorney Smith of Messrs. Bicksler, Smith & Parke appearing as counsel for the defendant and said Attorney Smith having argued in support of demurrer and said Attorney Cosgrove having argued in opposition to demurrer, it is by the court ordered that said demurrer be overruled, and exception having been reserved for the defendants, it is further ordered by the court that defendants herein have thirty (30) days to answer.

IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN  
DISTRICT OF CALIFORNIA,  
SOUTHERN DIVISION.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES, )	
Plaintiff, )	No. 1124 -- Civil.
- vs - )	
MARYLAND CASUALTY )	ANSWER TO
COMPANY, a Corporation, )	FIRST CAUSE OF
Defendant. )	ACTION

FIRST DEFENSE TO  
FIRST CAUSE OF ACTION

Comes now the defendant, and for answer and first defense to the first cause of action herein (the original complaint and amendment thereto), admits, denies and alleges as follows:

I.

For answer to the allegations of Paragraph V (amendment to complaint—first cause of action), defendant has no knowledge, information or belief sufficient to enable it to answer, and basing its denials upon that ground, denies that subsequent to the 26th day of December, 1919, and prior to the 3rd day of May, 1921, or at or upon or between any other two dates, or during the term of said bond, or beginning more particularly on or about the 19th day of November, 1920, or at any other time, or at various times, or at irregular intervals thereafter, up to and including about April 25, 1920, or until any other

period of time, plaintiff, in due and regular course of business, or otherwise, received eighty-seven drafts, or any other number of drafts drawn upon the California Cotton & Factorage Company, in the total amount of \$82,487.96, or any other sum of money. Upon the same ground denies that attached to said alleged eighty-seven drafts were one or more warehouse receipts, or any warehouse receipts, covering one or more bales of cotton; upon the same ground denies that there were attached to said alleged eighty-seven drafts a total of 1476, or any other number, of warehouse receipts, for 1476, or any other number of bales of cotton; upon the same ground denies that each or any of said alleged warehouse receipts had been, at the time of their alleged receipt by plaintiff, endorsed in blank by any person to whose order such receipt had been issued; and upon the same ground denies that said alleged receipts, or any of them, were, or that each was, negotiable and transferable upon delivery. Upon the same ground denies that immediately, or at any time, following the alleged receipt of each of said alleged drafts by plaintiff, or within four or five days thereafter, or at any other time, each of said drafts, or any of them, was accepted in writing by said California Cotton & Factorage Company, to-wit, by its Secretary, said J. B. Sears. Upon the same ground denies that immediately, or at any time, following said alleged several acceptances of said California Cotton & Factorage Company, plaintiff relied entirely thereon, and for no other reason, remitted and paid to the person or persons presenting said



drafts for acceptance and payment, the amount or face value thereof, or any amount or sum of money, in the alleged payment and satisfaction thereof; and upon the same ground denies that thereafter, or at any time, plaintiff carried upon its books and accounts as "bills receivable", or otherwise, all, or any, of said alleged drafts or acceptances alleged to have been so received and paid; upon the same ground denies that all, or any, of said warehouse receipts alleged to have been attached to said drafts or acceptances, were held by plaintiff as collateral, or other, security for the alleged payment of said California Cotton & Factorage Company of all, or any, of said alleged drafts or acceptances. Upon the same ground denies that the total face value of said alleged eighty-seven drafts was the sum of \$82,487.96, or any other sum of money, and denies that plaintiff paid, or advanced, said sum, or any other sum, to the various, or other persons presenting the same.

## II.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations contained in Paragraph 6 of the Amendment to Complaint—First Cause of Action, and basing its denials upon that ground, denies that at various, or any time, between November 19th, 1920, and April 25th, 1921, or upon or between any other two dates, the said J. B. Sears with the intent of fraudulently and dishonestly converting, misappropriating, embezzling and wilfully misapplying said alleged warehouse receipts, or any of them, or the cotton represented thereby, or any money

or proceeds obtained therefrom, and/or with the further alleged fraudulent and dishonest intent of causing a loss to said California Cotton & Factorage Company of any money, securities or personal property for which said California Cotton & Factorage Company would be responsible to plaintiff, said J. B. Sears applied to, or that he secured from plaintiff, all or any of the warehouse receipts then in its possession, and alleged to be held as collateral security for the payment of said alleged drafts and acceptances; upon the same ground denies that at said time, or at any time, and/or as part of said alleged transaction, and/or in acknowledgment of the delivery to said J. B. Sears of said alleged warehouse receipts, the said J. B. Sears executed or delivered to plaintiff eighty-seven, or any other number of trust receipts; upon the same ground defendant denies that the document quoted in said paragraph was, or is, the trust receipt alleged to have been so executed and given to plaintiff by said J. B. Sears. Upon the same ground denies that the said J. B. Sears, at the time he is alleged to have received said warehouse receipts, or executed and delivered said trust receipts, represented or stated to plaintiff, and/or its officers or agents, that in order to make and complete sales of cotton covered by said alleged warehouse receipts that it would be necessary to surrender said warehouse receipts, or any of them, to the persons, firms or corporations issuing the same, and/or to obtain possession of and deliver said cotton to the common carriers of freight over which shipments of said cotton would be made to the purchaser

thereof; upon the same ground denies that upon any alleged exchange being so made, the said J. B. Sears stated and represented that immediately after so surrendering said warehouse receipts, and securing or obtaining possession of and delivery of the cotton, that he would immediately thereafter return the bills of lading to plaintiff and take up said alleged trust receipt, or receipts, alleged to have been given by said J. B. Sears to plaintiff, at the time of, or in acknowledgment of the delivery to said J. B. Sears of warehouse receipts alleged to cover cotton alleged to have been so sold as aforesaid.

Upon the same ground defendant denies that in said alleged manner, and/or pursuant to said alleged fraudulent and dishonest plans or schemes, the said J. B. Sears procured from plaintiff between the 19th day of November, 1919, and the 25th day of April, 1921, or upon or between any other two dates, 1476, or any other number of warehouse receipts, for 1476 bales or any other number of bales, of cotton, and/or that he issued or caused to be issued or delivered to plaintiff in acknowledgment thereof, eighty-seven, or any other number, of said trust receipts.

### III.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations contained in Paragraph 7 of the Amendment to Complaint—First Cause of Action, and basing its denials upon that ground, denies that subsequent to the 19th day of November, 1920, and prior to the 3rd day of May, 1921, or at any other time, and/or at various



or any, times between said two dates, the said J. B. Sears without the knowledge of said California Cotton & Factorage Company, and/or pursuant to said alleged fraudulent or dishonest plan and scheme converted, mis-appropriated, embezzled, and/or wilfully misapplied 1091, or any other number, of said alleged 1476 warehouse receipts, and/or 1091, or any other number of bales of cotton represented thereby; upon the same ground denies that said J. B. Sears, sold said cotton, or any portion thereof, covered by said alleged warehouse receipts, to various, or any, purchasers of cotton throughout the United States; and upon the same ground denies that he surrendered said warehouse receipts, or any of them, to the persons or corporations issuing the same, and/or that he secured possession thereof, or delivered cotton alleged to have been represented thereby to common carriers of freight at any point in the State of California and Arizona for shipment and delivery to the purchasers thereof; and/or that he received from said common carriers any bills of lading for said alleged shipments of cotton. Upon the same ground denies that said J. B. Sears, at any time thereafter, and/or in violation of his alleged duties as Secretary of said California Cotton & Factorage Company, and/or in the alleged wilful violation of his alleged promises and/or representations to the plaintiff and/or in the alleged violation of the terms of said trust receipts alleged to have been delivered to to him by plaintiff, and/or pursuant to said alleged fraudulent and dishonest plan and scheme alleged herein, attached said bills of lading, or any of them, to a sight draft, or sight drafts alleged to have



been prepared by said J. B. Sears and drawn upon the alleged purchasers of said Cotton by said California Cotton & Factorage Company, in favor of the Citizens National Bank of Los Angeles, or any other person, and presented said sight draft, or drafts, with any bill of lading, or bills of lading, attached, for approval, acceptance or immediate issuance of credit thereon, to any officer of the plaintiff, or any officer other than the officers from whom it is alleged said J. B. Sears had obtained said alleged warehouse receipts and/or to whom he had delivered said trust receipts; and upon the same ground denies that said J. B. Sears, at said time, represented to said officer, or any officer, of plaintiff, to whom it is alleged said J. B. Sears delivered said sight draft, or drafts, and/or bills of lading, that the cotton, or any part thereof, covered by said alleged sight drafts and bills of lading was cotton belonging to said California Cotton & Factorage Company, and/or over which he had unrestricted right of disposal; upon the same ground denies that said J. B. Sears failed to disclose to said officer, or any other officer, the fact that said bank held any trust receipts of said California Cotton & Factorage Company, alleged to have been given to said J. B. Sears, as thereinbefore alleged, alleged to cover the cotton described in said alleged bills of lading. Upon the same ground denies that said J. B. Sears deposited said sight drafts, or any of them, with any bills of lading attached thereto with said officer, or with any officer, of plaintiff, and/or that he received, at that time, or at any other time, from any officer of plaintiff, credit upon the account of said California Cotton & Fac-

torage Company, to the amount of said sight draft, or in any sum of money. Upon the same ground denies that at said time, or at any other time, said J. B. Sears presented to any teller of plaintiff, the bank pass book of said California Cotton & Factorage Company, and/or that there was entered therein by said teller, or any person for plaintiff, as a deposit in said plaintiff bank to the credit of the account of said California Cotton & Factorage Company, in an amount equal to the amount of said sight draft, or any other sum of money; upon the same ground denies that the said J. B. Sears immediately thereafter, or at any time, and/or in the alleged pursuance of said alleged fraudulent scheme, falsified the books and accounts, or any of them of said California Cotton & Factorage Company, by entering, or causing to be entered therein, the various, or any, amounts of money alleged to have been so received from the various, or any, alleged sales of cotton, as therein alleged, and/or that the various, or any, amounts shown as having been deposited, and the various, or any, credits entered as alleged therein upon the bank pass book of said California Cotton & Factorage Company, as moneys or funds belonging wholly or entirely, or at all, to said California Cotton & Factorage Company, and/or that he then and there, or willfully, or at all, failed to enter in said books of said California Cotton & Factorage Company any entry, or memorandum, showing the nature of the transactions, and/or the manner in which said alleged warehouse receipts had been secured, or that any trust receipts had been issued, or

that moneys and credits entered in said bank pass book were received, as alleged therein; and upon the same ground denies that said J. B. Sears wilfully, or at all, failed to make, or cause to be made, any other entry or memorandum indicating that said funds of money, or any portion thereof, were charged with any trust, or were in any manner money, or funds, other than the absolute and unincumbered property and funds of said California Cotton & Factorage Company.

Upon the same ground denies that during and following said alleged transaction, or at any other time, the said J. B. Sears frequently, or at all, represented to said California Cotton & Factorage Company, its officers and directors, or any of them, that said alleged various, or any, sums of money and credits alleged to have been entered upon said pass book, and books of account of said California Cotton & Factorage Company were funds and money of said California Cotton & Factorage Company, and/or made or accumulated by the said J. B. Sears in the conduct of the affairs of said California Cotton & Factorage Company. Upon the same ground denies that said J. B. Sears, upon inquiry, represented and stated to plaintiff and/or its officers, or any of them, between said dates, or at any other time, that said California Cotton & Factorage Company still had and retained, or that said J. B. Sears still had in his custody in the vaults and files of said California Cotton & Factorage Company, all, or any, of the alleged warehouse receipts alleged to have been so surrendered to him by plaintiff. Upon the same ground denies that said California Cotton &



Factorage Company and/or plaintiff, and the directors and officers, or any of them, of each of said corporations, believed, acted upon and/or were deceived by said alleged dishonest and fraudulent representations of said J. B. Sears.

Upon the same ground denies that said alleged 1091 bales of cotton, or any other number of bales of cotton, were so disposed of by said J. B. Sears; and upon the same ground denies that said 1091 bales of cotton, or any portion thereof, was of the reasonable value of \$60,628.72, or any other sum of money; and upon the same ground denies that said sum, or any portion thereof, was credited to the account of said California Cotton & Factorage Company, either in the manner therein alleged, or at all.

#### IV.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations contained in Paragraph 8 of the Amendment to Complaint—First Cause of Action, and basing its denials upon that ground, denies that between November 19th, 1920, and May 3rd, 1921, or upon or between any other two dates, and/or pursuant to said alleged fraudulent and dishonest plan and scheme, and/or contemporaneous with the several, or other, conversions, misappropriations and embezzlements, that the said J. B. Sears, either fraudulently or dishonestly, or at all, converted, misappropriated, embezzled and/or wilfully misapplied the moneys and funds, or any of them or any money and funds alleged to have been placed to the credit of said California Cotton & Fac-



storage Company, either following the various alleged dishonest and fraudulent sales of cotton, or at all, and/or by using said alleged moneys and funds for the purpose of dealing and speculating in cotton, and/or conducting such dealings and speculations at a loss, and/or paying said alleged losses out of said money and funds, and/or in the payment of alleged credits and demands incurred by said J. B. Sears, in the said alleged dealings and speculations in cotton.

Upon the same ground denies that no part of said sum of \$60,628.72 was used by said J. B. Sears, or any other person, in the payment of any one, or more, of said alleged eighty-seven drafts or acceptances of said California Cotton & Factorage Company, alleged to have been held by plaintiff.

Upon the same ground denies that relying entirely, or at all, upon said alleged false and fraudulent representations of said J. B. Sears, and/or deceits alleged to have been practiced by him upon said California Cotton & Factorage Company and/or its officers and directors, that the said California Cotton & Factorage Company continued its business, and/or that it allowed and permitted said J. B. Sears subsequent to the 19th day of November, 1920 (improperly alleged in said amendment to the complaint, as 19th of November, 1921), and/or at any other time, and/or to continue to act as secretary, and/or to continue to perform the acts and things necessary to carry out the business of said California Cotton & Factorage Company, and/or that said California Cotton & Factorage Company and/or that said California Cotton & Factor-

age Company allowed and permitted said J. B. Sears to continue to deal and speculate in cotton and/or to continue to incur indebtedness or contract financial obligations in connection therewith. Upon the same ground denies that said California Cotton & Factorage Company, its directors and officers would not have continued its business subsequent to November 19th, 1920 (improperly alleged in said Amendment to Complaint as November 19th, 1921), nor would they have allowed said J. B. Sears to continue to act as Secretary of said California Cotton & Factorage Company after said date, or at any other time, nor would they, subsequent to said date, or at any other time, have allowed said J. B. Sears to conduct any alleged dealings and speculations in cotton or incurred indebtedness, or contract financial obligations upon its behalf, had it, or its officers, or any of them, other than said J. B. Sears, known of said alleged frauds, deceits, dishonesties and wrongful conversions, embezzlements, misappropriations, and/or wilful misapplications, or any of them, alleged to have been so practiced upon said California Cotton & Factorage Company, its officers, or any of them, or upon plaintiff.

V.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations contained in Paragraph 9 of the Amendment to Complaint—First Cause of Action, and basing its denials upon that ground, denies that due to, growing out of, or because of the alleged fraud, dishonesty, embezzlement, wrongful abstraction, and/or wilful misapplica-

tion of said alleged warehouse receipts, and/or the cotton, or any part thereof, alleged to have been so held thereunder, and/or bills of lading, or any of them, and/or the money, proceeds and credits alleged to have been realized from the alleged sales and disposition thereof by said J. B. Sears, that said California Cotton & Factorage Company has sustained a loss, and/or has become, and/or is responsible to plaintiff in the sum of \$60,628.72, or any other sum of money.

## VI.

For answer to the allegations of Paragraph 10 of the first cause of action, defendant denies that there was any fraudulent, dishonest or wilful misapplication of moneys, securities and personal property of said California Cotton & Factorage Company, in any wise, or at all, by the said J. B. Sears; denies that immediately upon the discovery of said alleged loss of said California Cotton & Factorage Company it notified the Maryland Casualty Company, and denies that it notified the Maryland Casualty Company within ten (10) days, and avers that the verbal notice to defendant of said alleged loss was more than twenty-one (21) days after the discovery of the loss alleged to have been sustained by the California Cotton & Factorage Company, through the alleged acts of said J. B. Sears.

Defendant avers that on or about ninety (90) days from April 28th, 1921, it received a verified itemized statement alleged to have been the loss sustained by said California Cotton & Factorage Company.



Defendant avers it has no knowledge, information or belief sufficient to enable it to answer the allegations that said alleged itemized statement contained a correct statement of any such alleged loss by said California Cotton & Factorage Company, through the acts of said J. B. Sears; and upon the same ground denies that said itemized statement is true and correct; and upon the same ground denies that it contains a statement showing all, or any, of the loss alleged to have been sustained by said California Cotton & Factorage Company, through the acts of said J. B. Sears; and upon the same ground denies that there was any loss sustained or liability incurred by said California Cotton & Factorage Company, through the alleged acts of said J. B. Sears, as aforesaid; and upon the same ground denies that said California Cotton & Factorage Company has sustained any loss to others under the terms of said bond by reason of the alleged fraud, dishonesty, embezzlement, wrongful abstraction and alleged wilful misapplication by said J. B. Sears, while employed by said California Cotton & Factorage Company.

## VII.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations of Paragraph 12 of the first cause of action, and basing its denials upon that ground denies that on or about the first day of December, 1921, or at any other time, the said California Cotton & Factorage Company, by an instrument in writing, or otherwise, assigned or transferred or set over to plaintiff all or any of its alleged



right, title or interest in and to said bond described in the complaint and/or in all or any of the moneys alleged to be due or become due, and/or including any or all claims, demands, causes of action or choses in action, in any or every clause, article or thing in said bond contained.

## SECOND DEFENSE TO FIRST CAUSE OF ACTION

For a further, separate and second defense to the First Cause of Action, Defendant adopts the allegations of its First Defense to the First Cause of Action herein and makes the same a part hereof, as though fully and entirely set forth herein at length, and further alleges:

### I.

That for the purpose of obtaining the bond sued upon herein, said California Cotton & Factorage Company made application in writing, a copy of which is attached to the answer of defendant to the Second Cause of Action herein, marked "Exhibit A," made a part thereof, and is hereby referred to, adopted and made a part hereof, as though fully and entirely set forth herein at length.

### II.

Defendant avers that it is provided in Paragraph 7, subdivision b, of said application, Exhibit A, which at all of the times alleged herein was, and is, part of the contract between the California Cotton & Factorage Company and this defendant, that there was "no cash in personal control (of said J. B. Sears) only as checks may be issued or received for deposit"; but

defendant is informed and believes and upon that ground avers the facts to be that the said J. B. Sears, with the knowledge and consent of said California Cotton & Factorage Company, and of its officers, handled all of the cash of said California Cotton & Factorage Company for such use and purposes as he, the said J. B. Sears, deemed best; and upon the same ground avers that with the knowledge and consent of said California Cotton & Factorage Company, and its officers, all of the cash of said corporation was handled by said J. B. Sears without being required to render any account for the same; and without being required by said California Cotton & Factorage Company, and its officers, to make any audit of all or any of said cash so handled, and without any process of book-keeping, so as to furnish in anywise, or at all, information to this defendant what became of said sums of money; and upon the same ground defendant avers that all of said sums of money so handled by said J. B. Sears were used in and for the purchase of cotton and other commodities for and on behalf of, and which became the property of said California Cotton & Factorage Company, and for the purpose of paying the expenses and cost of operation of said California Cotton and Factorage Company.

### III.

Defendant avers that pursuant to said application, Exhibit A to said answer to the Second Cause of Action, Paragraph 8, subdivision a, it is provided that "all things paid by check"; that defendant is informed and believes that with the knowledge and consent of

said California Cotton & Factorage Company, and its officers, the said J. B. Sears was permitted to use and did use the cash of said latter corporation in such manner as he deemed best.

IV.

Defendant further avers that pursuant to said application, Exhibit A aforesaid, Paragraph 12, subdivisions a and d, the books and accounts of said California Cotton & Factorage Company were to be "checked up at least once in each month" by "T. J. West, Treasurer"; but defendant is informed and believes and upon that ground avers the facts to be, that no audit whatsoever at any time was made of the books, accounts, stocks and securities of said California Cotton & Factorage Company, by any person; and upon the same ground avers that no inspection, audit or verification of the funds on hand, or in bank, of said California Cotton & Factorage Company, was made at any time by said latter corporation, or its officers, agent or any other person or persons; that if an audit had been made each month, as provided in the contract between the California Cotton & Factorage Company and defendant it would have revealed the facts, and if any loss had been sustained said loss could have been checked, lessened and stopped.

V.

Defendant further avers that it is provided in said application for the bond sued upon herein, (and which was duly signed on or about November 28th, 1919, by said California Cotton & Factorage Company): "It is agreed that the above answers are warranties



and constitute the basis of and form a part of the consideration of the bond executed or about to be executed by the Maryland Casualty Company in favor of the undersigned upon the person above named, and also all continuations or renewals thereof or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by the said Company”.

Defendant further avers that it is provided in said bond sued upon herein “that all ‘statements’ which the employer has furnished to the company (meaning defendant herein) concerning the employee (meaning said J. B. Sears) or his duties or accounts are ‘warranted’ by the employer to be true.”

That said statements and warranties referred to and quoted from defendant’s said bond, and said statements and warranties referred to and quoted from the application (or statement) of said California Cotton & Factorage Company expressly refer, among other things, to the answers in said application (or statement) of said California Cotton & Factorage Company. The copy of said application (or statement) of said California Cotton & Factorage Company is hereto attached, marked “Exhibit A”, and made a part hereof.

Defendant, therefore, further avers that the warranties in and by said application so signed by said California Cotton & Factorage Company, as aforesaid, and which became, were and are a part of the bond sued upon herein, and warranted by the employer to be true, were untrue, and broken in each and all



of the respects hereinbefore set forth, and that because thereof this defendant is released from any and all obligations and liability upon or under said bond.

Defendant further avers that the loss, if any, accruing to said California Cotton & Factorage Company (which defendant has fully denied) was with full knowledge of said California Cotton & Factorage Company, its officers and agents, at the time of said loss and/or losses; and especially with the knowledge, consent and acts of the said J. B. Sears; that said breaches of said warranties, as hereinbefore specified and set forth, were and are contrary to and in violation of the terms of said application (or signed statement), Exhibit "A" herein, and of the terms of defendant's said bond; and that said breaches of said warranties produced, and were the cause of, the loss, if any, sustained by plaintiff's assignor, said California Cotton & Factorage Company, and that said loss, if any, would and could not have occurred if said warranties hereinbefore set forth had not been broken.

### THIRD DEFENSE TO FIRST CAUSE OF ACTION.

For a further, separate and third defense to the First Cause of Action, defendant adopts the allegations of its first defense to the First Cause of Action herein, and makes the same a part hereof, as though fully and entirely set forth herein at length, and further alleges:

#### I.

That it is provided in said bond, paragraph 2, that within ten (10) days after said employer (California

Cotton & Factorage Company) had knowledge of, or became aware of any act of fraud or dishonesty committed by the employee (said J. B. Sears), while in the service of said corporation, that said California Cotton & Factorage Company would notify defendant herein by registered letter addressed to the defendant at its home office at Baltimore, Maryland, and also send such notice by telegram within ten days after said discovery; but defendant avers that no notice, knowledge or information was furnished to defendant either by said California Cotton & Factorage Company, or at all, for more than twenty-one (21) days after the alleged acts of fraud, dishonesty, wrongful abstraction and wilful misapplication by said J. B. Sears.

#### FOURTH DEFENSE TO FIRST AND SECOND CAUSES OF ACTION.

For a further, separate and fourth defense to the first cause of action and the second cause of action, defendant adopts the allegations of its first defense to the First Cause of Action herein, and makes the same a part hereof, as though fully and entirely set forth herein at length, and further alleges:

##### I.

Defendant is informed and believes, and upon that ground avers the facts to be that said California Cotton & Factorage Company was organized under the laws of the State of California, on or about August 12th, 1919, with an authorized capital of \$50,000.00, and that the officers thereof were as follows:

T. W. McDevitt, President,

C. W. Hartke, Vice President,

J. B. Sears, Secretary,

T. J. West, Treasurer.

And that said directors were as follows:

T. W. McDevitt,

C. W. Hartke,

J. B. Sears,

T. J. West,

John P. Conduit.

Upon the same ground defendant avers that no stock was issued by said corporation until on or about January 29th, 1920, when stock certificates were issued as follows:

496 Shares to said T. J. West,

1    "    "    "    T. W. McDevitt,

1    "    "    "    John P. Conduit,

1    "    "    "    J. B. Sears,

1    "    "    "    C. W. Hartke.

Upon the same ground defendant avers that on or about May 24th, 1920, the said T. J. West surrendered his said 496 shares of stock and that said 496 shares were issued to said J. B. Sears; and that one share was issued to said T. J. West on the same date, but that said certificate was never signed by the President of said California Cotton & Factorage Company.

Upon the same ground defendant avers that the said T. J. West surrendered all of his said stock and that the same was cancelled without any consideration being paid to T. J. West for the surrender and cancellation of said stock and that on or about May 24th, 1920, it was known to the said California Cotton & Factorage Company, and all of its officers and agents



that the said J. B. Sears was the sole officer, manager and agent, and in charge of the entire business affairs of said California Cotton & Factorage Company; and that the same was being run at a loss; that cotton was depreciating in value; that debts and obligations to plaintiff herein and other corporations, partnerships and persons were being incurred and were due and unpaid and that all of the acts and conduct of the affairs of the said California Cotton & Factorage Company by said J. B. Sears were at all of said times understood and fully known by said California Cotton & Factorage Company, and its officers and agents.

That on and after May 24th, 1920, the said J. B. Sears became and was the practical owner of the entire assets and business of said California Cotton & Factorage Company, and that for all practical purposes, that on and after said last mentioned date, said California Cotton & Factorage Company became and was a "Corporation Sole", to-wit, the said J. B. Sears, and that said corporation continued to act as a "Corporation Sole," to-wit, J. B. Sears, from and after May 24th, 1920, until on or about May 3rd, 1921, when the said J. B. Sears died.

#### FIFTH DEFENSE TO FIRST CAUSE OF ACTION

For a further, separate and fifth defense to the first cause of action and the second cause of action, defendant adopts the allegations of its first defense to the first cause of action herein, and makes the same a part hereof, as though fully and entirely set forth herein at length, and further alleges:



## I.

Defendant is informed and believes, and upon that ground avers the facts to be, that all of the transactions of said California Cotton & Factorage Company, transacted with plaintiff, its officers and agents herein, were with the full knowledge of all the facts, stated and represented by said California Cotton & Factorage Company, its officers and agents, and that bills of lading, warehouse receipts and/or other evidences or indicia of ownership in and to the title of cotton purchased by said California Cotton & Factorage Company, of which plaintiff held said evidence or indicia of ownership, warehouse receipts, or otherwise, were voluntarily surrendered by plaintiff, and plaintiff's lien or claim of lien thereto extinguished; and upon the same ground alleges that upon the resale by said California Cotton & Factorage Company, and its officers and agents, of each and all of said cotton so evidenced by said warehouse receipts, bills of lading and other indicia of ownership, that said warehouse receipts and bills of lading upon said resale were returned to and delivered to plaintiff, its officers and agents, and that plaintiff received payment for said cotton so resold by said California Cotton & Factorage Company, its officers and agents, and that therefore plaintiff sustained no loss whatever by or through any alleged fraud or dishonestly converting, misappropriating, embezzling or wilfully misapplying any of said bills of lading, warehouse receipts, or other evidences of title, by said J. B. Sears.



## EXHIBIT "A"

## EMPLOYER

No.....

FIDELITY SECTION  
 BONDING DEPARTMENT  
 MARYLAND CASUALTY COMPANY  
 BALTIMORE

.....19....

California Cotton & Factorage Co.  
 548 Merchants National Bank Bldg.,  
 Los Angeles, Calif.

An Application has been made to this Company to issue to you a Fidelity Bond for Mr. J. B. Sears as Secretary & Manager in your service, at Los Angeles, Calif., to the amount of \$50,000.00.

Before passing on the said Application the Company must have answers to the following questions:

Very respectfully yours,  
 F. Highlands Burns,  
 President

## ANSWERS

## QUESTIONS

- 1 To whom is the bond to be made payable?  
 (a). Give exact title.  
 (b). State Employer's line of business.
- 2 From what date is it to be written and for what amount?

a California Cotton & Factorage Co.  
 b Buying and selling cotton.

From Nov. 1st, 1919, for \$50,000.00

- 3 (a). What is the title of the applicant's position?  
(b). If traveling salesman, who will pay his traveling expenses?  
(c). At what place will he be employed?  
(d). Explain fully his duties.
  - 4 Who will pay the premium on the bond?
  - 5 (a). From when does his present employment date?  
(b). Has the applicant previously been in your employ?  
(c). Has the applicant been under bond to you?  
(d). Why is change now desired?  
(e). Have you any knowledge or any information or are you aware of any habit of the applicant or any circumstances which might unfavorably affect the risk to the surety on the bond applied for? If so, state particulars.
- |   |                                   |   |                                      |
|---|-----------------------------------|---|--------------------------------------|
| a | Secretary & manager               | b | .....                                |
| c | Los Angeles, Calif.               | d | Will run the business                |
|   | California Cotton & Factorage Co. |   |                                      |
| a | Sept. 1st, 1919.                  | b | From...No..., 19..., to....., 19.... |
| c | ....., No..... Surety.....        | d | ....., No.....                       |
| e | None .....                        |   |                                      |



- 6 (a). If paid by salary, state amount and when payable.
- (b). If applicant will be remunerated by you on any other basis, state nature of the engagement, with amount of applicant's monthly earnings. (Attach copy of Contract, if any.)
- (c). If a salesman, will applicant be charged with any portion of losses arising from bad credits?
- (d). If a salesman, will he be required to remit all collections immediately to Home Office?
7. (a). If applicant's duties embrace the custody of Cash, state largest amount likely to be under his or her control at any one time.
- (b). For what length of time is applicant apt to have control of such amount?
- (c). Will applicant have control of securities?

- a \$5,000.00 per year payable monthly as a minimum guarantee on
- b 25% of the profits. Contract not yet drawn up.
- c .....
- d .....
- a Cash be in bank
- b No cash in personal control, only as checks may be issued or received for deposit.
- c .....

(d). If so, state value of same, whether negotiable, and if such securities are under joint control with some other officer.

8 (a). Will applicant be authorized to pay out of the Cash in his or her custody any amount on your account?

(b). In what manner is such authority given?

9 (a). If applicant's duties embrace custody of goods or samples, give particulars, stating probable maximum value.

(b). How often, in what manner, and by whom will inventory of such stock of goods and samples be taken?

NOTE:—It is necessary that this

d Negotiable all of them and under his control.

a All things paid by check

b By-laws.

a .....

b ..... (OVER)  
"Exhibit A"

Bond cannot be executed until this form is fully completed and returned to the Company.

NOTE:—It is necessary that this form be fully completed  
QUESTIONS  
ANSWERS

- 10 (a). How often and to whom will applicant remit or pay over money received?  
 (b). Will applicant be permitted to retain any balance on hand; if so, about how much, and for what purpose?  
 (c). If required to deposit in Banks, state in what name accounts will be kept.  
 (d). Will applicant or the Bank be required to send you duplicate deposit slips or receipts?  
 (e). State whether applicant can endorse checks drawn to your order, and for what purpose.
- 11 (a). Will applicant be authorized to sign checks on your behalf?  
 (b). Will the countersignature of any other person be invariably required; if so, whose?

a Money be deposited as received.

b No cash except in bank.

c California Cotton & Factorage.

d .....

e Yes for deposit.

a Yes he is manager.

b No the owners live in other cities.

- 12 (a). At what intervals will applicant's books, accounts, stock and securities be inspected and audited and verified with funds on hand or in bank?
- (b). At what intervals and in what manner will outstanding accounts, as shown by applicant's books or reports, be verified?
- (c). If salesman or collector, how often do you bill the trade direct?
- (d). By whom will above inspections and audits be made?
- 13 (a). Has applicant always faithfully, honestly and punctually accounted to you for all moneys and property heretofore under his control or custody as your employee?

a. At least once in every Books checked up each month months.

b. At least once in every We have no such accounts. months.

c . . . . .

d T. J. West Treasurer . . . . . official capacity.

a Yes.



(b). Are applicant's accounts at this date in every respect correct, and proper securities, property and funds on hand to balance his accounts?

b Yes.  
a No.

14 (a). Is applicant now in debt to you?  
(b). If so, state amount and nature of such indebtedness, and if secured, how?

b .....

15 Have you ever sustained loss through the dishonesty of any one holding the position of the applicant, or holding a similar position?

No.

16 (a). Will you require additional surety from the applicant other than the amount applied for to this Company?

a No.

(b). If so, state amount, and by whom given?

b .....

It is agreed that the above answers are warranties and constitute the basis of and form a part of the consideration of the bond executed or about to be executed by the MARYLAND CASUALTY COMPANY in favor of the undersigned upon the person above named, and also all continuations or renewals thereof or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by the said Company.

Dated at Calexico, Calif., this 28th day of November, 1919.

Signature of employer CALIFORNIA COTTON &  
FACTORAGE CO.

By T. J. West

Treasurer Official Capacity.

If the employer (the obligee in the bond) be an individual, he must sign this statement; if a firm, one of the firm must sign the firm name and his own; if a corporation, it must be signed by an executive officer and returned to the Home Office of the Company at Baltimore, Md.

[Endorsed]: (ORIGINAL) No. 1124—Civil. In The UNITED STATES DISTRICT COURT In and for the Southern District of California, SOUTHERN DIVISION. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff —vs— MARYLAND CASUALTY COMPANY, a Corporation, Defendant. ANSWER TO FIRST CAUSE OF ACTION FOURTH DEFENSE TO SECOND CAUSE OF ACTION. Received copy of the within Answer this 5th day of November 1922 Hunsaker, Britt & Cosgrove attorney for Plaintiff FILED DEC 6 1922. CHAS. N. WILLIAMS, Clerk By L J Cordes BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant.

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IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

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THE CITIZENS NATIONAL )  
BANK OF LOS ANGELES, )

Plaintiff, )

—vs— )

MARYLAND CASUALTY )  
COMPANY, a Corporation, )

Defendant. )

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No. 1124—Civil

ANSWER

FIRST DEFENSE TO SECOND CAUSE  
OF ACTION

Now comes defendant, and for answer to the allegations of the second alleged cause of action herein, admits, denies and alleges as follows:

I.

For answer to the allegations of Paragraph 10 of the first cause of action (adopted in Paragraph 1 of the second cause of action), defendant denies that there was any fraudulent, dishonest or wilful misapplication of moneys, securities and personal property of said California Cotton & Factorage Company, in any wise, or at all, by the said J. B. Sears; denies that immediately upon the discovery of said alleged loss of said California Cotton & Factorage Company it notified the Maryland Casualty Company, and denies that it notified the Maryland Casualty Company within ten (10) days, and avers that the verbal notice to defendant of said alleged loss was more than twenty-one (21) days after the discovery of the loss alleged to have been sustained by the California Cotton & Factorage Company, through the alleged acts of said J. B. Sears.

Defendant avers that on or about Ninety (90) days from April 28th, 1921, it received a verified itemized statement alleged to have been the loss sustained by said California Cotton & Factorage Company.

Defendant avers it has no knowledge, information or belief sufficient to enable it to answer the allegations that said alleged itemized statement contained a correct statement of any such alleged loss by said California Cotton & Factorage Company, through the acts of said J. B. Sears; and upon that ground denies that said itemized statement is true and correct; and upon the same ground denies that it contains a state-



ment showing all, or any, of the loss alleged to have been sustained by said California Cotton & Factorage Company, through the acts of said J. B. Sears; and upon the same ground denies that there was any loss sustained or liability incurred by said California Cotton & Factorage Company, through the alleged acts of said J. B. Sears, as aforesaid; and upon the same ground denies that said California Cotton & Factorage Company has sustained any loss to others under the terms of said bond by reason of the alleged fraud, dishonesty, embezzlement, wrongful abstraction and alleged wilful misapplication by said J. B. Sears, while employed by said California Cotton & Factorage Company.

## II.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations of Paragraph 12 of the first cause of action, (adopted in Paragraph 1 of the second cause of action) and basing its denials upon that ground denies that on or about the first day of December, 1921, or at any other time, the said California Cotton & Factorage Company, by an instrument in writing, or otherwise, assigned or transferred or set over to plaintiff all or any of its alleged right, title or interest in and to said bond described in the complaint and/or in all or any of the moneys alleged to be due or become due, and/or including any or all claims, demands, causes of action or choses in action, in any or every clause, article or thing in said bond contained.

III.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations of Paragraph 2 of the second cause of action, and basing its denials upon that ground, denies that between December 26th, 1919 and May 3, 1921, or upon or between any other two dates, or at any time, or during the term of said bond, or while the same was in full force and effect, the said J. B. Sears fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and wilfully misapplied any funds of said California Cotton & Factorage Company to his own use and purposes; upon the same ground denies that the said J. B. Sears fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and wilfully misapplied the money and funds of the California Cotton & Factorage Company without the knowledge of said California Cotton & Factorage Company, its officers and agents; upon the same ground denies that the said J. B. Sears fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and wilfully misapplied any of the money or funds of said California Cotton & Factorage Company, either in the amount of \$5,503.88, or in any other sum of money, to his own use and purposes, or to the use and purpose of any corporation, partnership or individual, other than said California Cotton & Factorage Company; and upon the same ground denies that said J. B. Sears fraudulently, dishonestly, wrongfully and wilfully embezzled, wrongfully abstracted and/or wilfully misapplied any sum

of money of said California Cotton & Factorage Company in satisfaction of his personal obligations, or on account of his personal obligations; or at all; upon the same ground denies that said funds in the sum of \$5,503.88, or any other sum of money, were by said J. B. Sears withdrawn from the moneys and funds of said California Cotton & Factorage Company in the possession of said J. B. Sears, or withdrawn from deposit with the Citizens National Bank of Los Angeles, and used in any other way or manner than to the use of and for the benefit of the California Cotton & Factorage Company.

#### IV.

Defendant has no knowledge, information or belief sufficient to enable it to answer the allegations of Paragraph 3 of the second cause of action, and basing its denials upon that ground, denies that due to or growing out of, or because of said alleged fraud, dishonesty, embezzlement, wrongful abstraction and said alleged wilful misapplication by the said J. B. Sears, of any money or funds of the said California Cotton & Factorage Company, that the said latter corporation has sustained a loss in the sum of \$5,503.88, or in any other sum of money.

#### SECOND DEFENSE TO SECOND CAUSE OF ACTION

FOR A FURTHER, SEPARATE AND SECOND DEFENSE TO THE SECOND CAUSE OF ACTION, DEFENDANT ADOPTS THE ALLEGATIONS OF ITS FIRST DEFENSE TO THE SECOND CAUSE OF ACTION AND MAKES THE



SAME A PART HEREOF, AS THOUGH FULLY AND ENTIRELY SET FORTH HEREIN AT LENGTH, AND FURTHER ALLEGES:

I.

That for the purpose of obtaining the bond sued upon herein, the said California Cotton & Factorage Company made application in writing, a copy of which is hereto attached, marked "Exhibit A", and expressly made a part hereof.

II.

Defendant avers that it is provided in Paragraph 7, subdivision 1, of said application, Exhibit A, which at all of the times alleged herein was, and is, part of the contract between the California Cotton & Factorage Company and this defendant, that there was "no cash in personal control (of said J. B. Sears) only as checks may be issued or received for deposit"; but defendant is informed and believes and upon that ground avers the facts to be that the said J. B. Sears, with the knowledge and consent of said California Cotton & Factorage Company, and of its officers, handled all of the cash of said California Cotton & Factorage Company for such use and purposes as he, the said J. B. Sears, deemed best; and upon the same ground avers that with the knowledge and consent of said California Cotton & Factorage Company, and its officers, all of the cash of said corporation was handled by said J. B. Sears without being required to render any account for the same; and without being required by said California Cotton & Factorage Company, and its officers, to make any audit



of all or any of said cash so handled, and without any process of bookkeeping, so as to furnish in anywise, or at all, information to this defendant what became of said sums of money; and upon the same ground defendant avers that all of said sums of money so handled by said J. B. Sears was used to pay petty and other expenses of the said California Cotton & Factorage Company, and not otherwise.

### III.

Defendant avers that pursuant to said application, Exhibit A herein, paragraph 8, subdivision a, it is provided that "all things paid by check" that defendant is informed and believes that with the knowledge and consent of said California Cotton and Factorage Company, and its officers, the said J. B. Sears was permitted to use and did use the cash of said latter corporation in such manner as he deemed best.

### IV.

Defendant further avers that pursuant to said application, Exhibit A, Paragraph 12, subdivision a, the books and accounts of said California Cotton & Factorage Company were to be checked up at least once each month; but defendant is informed and believes, and upon that ground avers the facts to be, that no audit whatsoever at any time was made of the books, accounts, stocks and securities of said California Cotton & Factorage Company; and upon the same ground avers that no inspection, audit or verification of the funds on hand, or in bank, of said California Cotton & Factorage Company, was made at any time by said latter corporation, or its officers;

that if an audit had been made each month, as provided in the contract between the California Cotton & Factorage Company and defendant it would have revealed the facts, and if any loss had been sustained said loss could have been checked, lessened and stopped.

THIRD DEFENSE TO SECOND CAUSE  
OF ACTION.

FOR A FURTHER, SEPARATE AND THIRD DEFENSE TO THE SECOND CAUSE OF ACTION, DEFENDANT ADOPTS THE ALLEGATIONS OF ITS FIRST DEFENSE TO THE SECOND CAUSE OF ACTION AND MAKES THE SAME A PART HEREOF, AS THOUGH FULLY AND ENTIRELY SET FORTH HEREIN AT LENGTH, AND FURTHER ALLEGES:

I.

That it is provided in said bond, paragraph 2, that within ten (10) days after said employer (California Cotton & Factorage Company) had knowledge of, or became aware of any act of fraud or dishonesty committed by the employee (said J. B. Sears), while in the service of said corporation, that said California Cotton & Factorage Company would notify defendant herein by registered letter addressed to the defendant at its home office at Baltimore, Maryland, and also send such notice by telegram within ten days after said discovery; but defendant avers that no notice, knowledge or information was furnished to defendant either by said California Cotton & Factorage Com-

pany, or at all, for more than twenty-one (21) days after the alleged acts of fraud, dishonesty, wrongful abstraction and wilful misapplication by the said J. B. Sears.

WHEREFORE, defendant prays judgment dismissing the complaint herein, and for its costs herein incurred; and for such other and further relief as it may, in law and equity, be found entitled.

Bicksler, Smith & Parke,

Attorneys for Defendant...

# EXHIBIT "A"

EMPLOYER

FIDELITY SECTION  
BONDING DEPARTMENT  
MARYLAND CASUALTY COMPANY  
BALTIMORE

No.....

California Cotton & Factorage Co.  
548 Merchants National Bank Bldg.,  
Los Angeles, Calif.

.....19....

An Application has been made to this Company to issue to you a Fidelity Bond for Mr. J. B. Sears as Secretary & Manager in your service, at Los Angeles, Calif., to the amount of \$50,000.00.

Before passing on the said Application the Company must have answers to the following questions:

Very respectfully yours,  
F. Highlands Burns,  
President

## ANSWERS

## QUESTIONS

- 1 To whom is the bond to be made payable?  
(a). Give exact title.  
(b). State Employer's line of business.
- 2 From what date is it to be written and for what amount?

- a California Cotton & Factorage Co.
- b Buying and selling cotton.

From Nov. 1st, 1919, for \$50,000.00



- 3 (a). What is the title of the applicant's position?  
 (b). If traveling salesman, who will pay his traveling expenses?  
 (c). At what place will he be employed?  
 (d). Explain fully his duties.
- 4 Who will pay the premium on the bond?
- 5 (a). From when does his present employment date?  
 (b). Has the applicant previously been in your employ?  
 (c). Has the applicant been under bond to you?  
 (d). Why is change now desired?  
 (e). Have you any knowledge or any information or are you aware of any habit of the applicant or any circumstances which might unfavorably affect the risk to the surety on the bond applied for? If so, state particulars.
- a Secretary & manager  
 b .....  
 c Los Angeles, Cal.  
 d Will run the business  
 California Cotton & Factorage Co.  
 a Sept. 1st, 1919.  
 b From...No..., 19..., to..., 19...  
 c.....No..... Surety.....  
 d .....  
 e None .....

- 6 (a). If paid by salary, state amount and when payable.  
(b). If applicant will be remunerated by you on any other basis, state nature of the engagement, with amount of applicant's monthly earnings. (Attach copy of Contract, if any.)  
(c). If a salesman, will applicant be charged with any portion of losses arising from bad credits?  
(d). If a salesman, will he be required to remit all collections immediately to Home Office?
7. (a). If applicant's duties embrace the custody of Cash, state **largest** amount likely to be under his or her control at any one time.  
(b). For what length of time is applicant apt to have control of such amount?  
(c). Will applicant have control of securities?
- a \$5,000.00 per year payable monthly as a minimum guarantee on  
b 25% of the profits. Contract not yet drawn up.  
c .....  
d .....  
a Cash be in bank  
b No cash in personal control, only as checks may be issued or received for deposit.  
c .....

(d). If so, state value of same, whether negotiable, and if such securities are under joint control with some other officer.

8 (a). Will applicant be authorized to pay out of the Cash in his or her custody any amount on your account?

(b). In what manner is such authority given?

9 (a). If applicant's duties embrace custody of goods or samples, give particulars, stating probable maximum value.

(b). How often, in what manner, and by whom will inventory of such stock of goods and samples be taken?

NOTE:—It is necessary that this

d Negotiable all of them and under his control.

a All things paid by check

b By-laws.

a .....

b ..... (OVER)  
"Exhibit A"

Bond cannot be executed until this form is fully completed and returned to the Company.

NOTE:—It is necessary that this form be fully completed  
QUESTIONS  
ANSWERS

- 10 (a). How often and to whom will applicant remit or pay over money received?  
(b). Will applicant be permitted to retain any balance on hand; if so, about how much, and for what purpose?  
(c). If required to deposit in Banks, state in what name accounts will be kept.  
(d). Will applicant or the Bank be required to send you duplicate deposit slips or receipts?  
(e). State whether applicant can endorse checks drawn to your order, and for what purpose.
- 11 (a). Will applicant be authorized to sign checks on your behalf?  
(b). Will the countersignature of any other person be invariably required; if so, whose?

a Money be deposited as received.

b No cash except in bank.

c California Cotton and Factorage.

d .....

e Yes for deposit.

a Yes he is manager.

b No the owners live in other cities.



- 12 (a). At what intervals will applicant's books, accounts, stock and securities be inspected and audited and verified with funds on hand or in bank?
- (b). At what intervals and in what manner will outstanding accounts, as shown by applicant's books or reports, be verified?
- (c). If salesman or collector, how often do you bill the trade direct?
- (d). By whom will above inspections and audits be made?
- 13 (a). Has applicant always faithfully, honestly and punctually accounted to you for all moneys and property heretofore under his control or custody as your employee?
- a Yes.
- a. At least once in every Books checked up each month months.
- b. At least once in every We have no such accounts. months.
- c . . . . .
- d T. J. West Treasurer . . . . . official capacity.

(b). Are applicant's accounts at this date in every respect correct, and proper securities, property and funds on hand to balance his accounts?

b Yes.  
a No.

14 (a). Is applicant now in debt to you?  
(b). If so, state amount and nature of such indebtedness, and if secured, how?

b .....

15 Have you ever sustained loss through the dishonesty of any one holding the position of the applicant, or holding a similar position?

No.

16 (a). Will you require additional surety from the applicant other than the amount applied for to this Company?

a No.

(b). If so, state amount, and by whom given?

b .....

It is agreed that the above answers are warranties and constitute the basis of and form a part of the consideration of the bond executed or about to be executed by the MARYLAND CASUALTY COMPANY in favor of the undersigned upon the person above named, and also all continuations or renewals thereof or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by the said Company.

Dated at Calexico, Calif., this 28th day of November, 1919.

Signature of employer CALIFORNIA COTTON &  
FACTORAGE CO.

By T. J. West

Treasurer Official Capacity.

If the employer (the obligee in the bond) be an individual, he must sign this statement; if a firm, one of the firm must sign the firm name and his own; if a corporation, it must be signed by an executive officer and returned to the Home Office of the Company at Baltimore, Md.

STATE OF CALIFORNIA, County of Los Angeles. ss.

E. F. KRAEMER, being by me first duly sworn deposes and says: That he is the agent and manager of the Southern California claim Division of defendant corporation in the above entitled action; that he has read the foregoing Answer and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information or belief, and as to those matters that he believes it to be true.

E. F. Kraemer.

Subscribed and sworn to before me this 31st day of August 1922.

(SEAL)

W. C. Smith

Notary Public in and for the County of Los Angeles,  
State of California.

[Endorsed]: (ORIGINAL) No 1124—Civil In The United States District Court In and for the Southern District of California, Southern division. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff,—vs— MARYLAND CASUALTY COMPANY, a Corporation, Defendant. ANSWER FILED AUG 31 1922 CHAS. N. WILLIAMS, Clerk By W. J. Tufts Deputy Clerk Received copy of the within Answer this 31st day of August 1922 Hunsaker, Britt & Cosgrove, Attorney for Plaintiff BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant.



IN THE UNITED STATES DISTRICT COURT,  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

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THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES, )	No. 1124-Civil
Plaintiff, )	SUPPLE-
—vs— )	MENTAL
MARYLAND CASUALTY )	ANSWER
COMPANY, a Corporation, )	Special Defense
Defendant. )	

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Now comes the defendant and for further answer to the complaint and the amendment thereto, and by way of special defense avers:

That it is provided in the bond, based upon which the suit herein has been brought, as follows:

“THIS BOND is executed upon the following express conditions: which are conditions precedent to the right of the Employer to recover hereunder:

. . . . .

“3. That any loss covered hereunder be discovered during the continuance of this bond or within six (6) months after its termination, and notice of such loss be sent by telegraph and by registered letter, both addressed to the Company at its Home Office, Baltimore, Maryland, within ten (10) days after the discovery; that an itemized statement of the loss shall be filed with the Company by the Employer within ninety (90) days after the date of said notice of loss; that if required by the company, the Employer

shall produce for investigation all books, vouchers and evidence in the Employer's possession, and render every assistance (except pecuniary) capable of being rendered by the Employer, that may aid in bringing the Employee to justice."

That the "Employer" above referred to, at all of the times herein alleged was, and is, said California Cotton & Factorage Company.

Defendant avers that on and before the filing of the complaint and subsequent thereto, it has made repeated demands upon said California Cotton & Factorage Company to inspect all books, papers, documents, vouchers, minutes and by-laws of said corporation, and correspondence of said corporation, for the purpose of making its defense, if any it had, herein; that at all of said time it has been promised full, fair and complete disclosure of all facts, and inspection of all of the aforesaid papers; that the last demand for said documents was made by this defendant to T. W. McDevitt, President of said company, on or about March 1st, 1923, at which time said documents were promised; but that almost nine months having elapsed after the first demand was made for said documents, and the day of trial being April 10th, 1923, and said documents not having been produced, defendant avers that the plaintiff has wilfully failed and refused to produce the minute book, if any, of said California Cotton & Factorage Company; and has wilfully failed and refused to produce the articles of incorporation, if any it has; and has wilfully failed and refused to produce any correspondence whatsoever

it has, or may have, pertaining to the issues involved in this case.

Defendant is informed and believes, and upon that ground avers the facts to be, that the said California Cotton & Factorage Company, its officers, manager and agents in control of its general and only office in the City of Los Angeles, California, has had, and now has, correspondence and letters from the plaintiff herein relating to the amounts owing by said California Cotton & Factorage Company to plaintiff, and the acts of said J. B. Sears, as alleged in the complaint and amendment thereto, and that plaintiff is informed that at all times on and after August 12th, 1919, and until the death of said J. B. Sears, said California Cotton & Factorage Company owed said bank large sums of money, the amount of which defendant is unable to fully state, solely because of the information which defendant alleges upon information and belief is contained in said letters, correspondence and notices by plaintiff to said California Cotton & Factorage Company, covering all of the period of time during which said California Cotton & Factorage Company transacted its said business, as alleged in the complaint and its amendment thereto, with the plaintiff, and that said California Cotton & Factorage Company, and the plaintiff herein, in and by said letters, correspondence and notices, as aforesaid, at all times had notice, knowledge and information of the facts as alleged in the complaint herein and the amendments thereto.



Defendant is informed and believes, and upon that ground avers that the said J. B. Sears was the sole manager and operator of the California Cotton & Factorage Company, and that said company had no meeting of its Board of Directors, and that said Company has no minutes; and that said persons alleged to have constituted the Board of Directors, other than said J. B. Sears, to-wit, T. W. McDevitt, C. H. Hartke, T. J. West and John P. Conduit, never met upon notice, or otherwise, as a Board of Directors of said corporation; and upon the same ground avers that said company has no minutes of any meetings of its alleged Board of Directors, and that its alleged Board of Directors has had no meeting; and that said J. B. Sears, as the sole manager and operator of said California Cotton & Factorage Company at all times had notice and knowledge of all acts and transactions by and between said California Cotton & Factorage Company and plaintiff herein.

That solely in and by the wilful failure and refusal of said California Cotton & Factorage Company to carry out the terms of the contract between the parties in said bond as above quoted, defendant is unable to, in all of the matters and things hereinbefore set forth, defend against the action set up in the complaint and the amendment thereto.

WHEREFORE defendant prays that because of the wilful breach of said contract between said California Cotton & Factorage Company and Defendant as hereinbefore set forth, and the wilful refusal of said California Cotton & Factorage Company to abide by its said



agreement and carry out the terms thereof, that this defendant be discharged from its said contract and that the complaint herein be dismissed and that defendant have judgment for its costs herein expended.

Bicksler, Smith & Parke.

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Attorneys for Defendant, Maryland  
Casualty Company, a Corp.

UNITED STATES OF AMERICA,     )  
Southern District of California,     ) SS.  
Southern Division.     )

W. C. SMITH, being by me first duly sworn, deposes and says: That he is one of the attorneys for the Maryland Casualty Company, a Corporation, defendant in the above entitled action; that he has read the foregoing Supplemental Answer, and knows the contents thereof; and that the same is true of his own knowledge, except as to the matters which are therein stated upon his information and belief, as to those matters he believes them to be true.

Affiant makes this affidavit for the reason that there is no officer of said defendant corporation within the jurisdiction of the Court.

W. C. Smith

Subscribed and sworn to before me this 6th day of March, 1923.

(Seal)

Myrtle M. Reeder

Notary Public in and for the County of Los Angeles,  
State of California.

[Endorsed]: (ORIGINAL) No. 1124—Civil In  
the UNITED STATES DISTRICT COURT In and

for the Southern District of California, SOUTHERN DIVISION. In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff —vs— MARYLAND CASUALTY COMPANY, a Corporation, Defendant. SUPPLEMENTAL ANSWER Special Defense Received copy of the within Supplemental Answer this 7th day of March 1923 Hunsaker, Britt & Cosgrove By J R C Attorney for Plaintiff. FILED MAR 9 1923 CHAS. N. WILLIAMS, Clerk By W. J. Tufts deputy clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg. Fifth & Spring Sts. Los Angeles, Cal. Telephone 10227; Main 5166 Attorneys for Defendant

At a stated term, towit: the January, A. D. 1923 Term of the District Court of the United States of America, within and for the Southern Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, on Monday, the nineteenth day of March, in the year of our Lord one thousand nine hundred and twenty-three;

Present: The Honorable Oscar A. Trippet, District Judge.

The Citizens National Bank of )	
of Los Angeles, )	
Plaintiff, )	
vs. )	No. 1124 Civil.
Maryland Casualty Co., a cor- )	
poration, )	
Defendant. )	

This cause coming on at this time for hearing on defendant's motion for leave to file supplementary An-

swer; Lyle Pendegast, Esq. appearing as counsel for the plaintiff and Attorney Parke of Messrs. Bicksler, Smith & Parke, appearing as counsel for the defendant, it is by the court ordered, plaintiff's counsel consenting thereto, that the motion of defendant to file supplementary answer be and the same is hereby granted.

No. 1124 Civil

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL )	
BANK, )	
Plaintiff, )	STIPULATION
V. )	WAIVING TRIAL
MARYLAND CASUALTY )	BY JURY
COMPANY, a corporation, )	
Defendant. )	

The parties in the above matter, acting by and through their respective attorneys of record, hereby specifically waive a jury in the trial of the above entitled cause and agree to a trial and submission of the same by the court without the intervention of a jury. Notice of the setting of said cause for trial on, to-wit, Tuesday, the 10th day of April, 1923, is hereby waived.

Hunsaker, Britt & Cosgrove,  
Attorneys for Plaintiff  
Bicksler, Smith & Parke  
Attorneys for Defendant

It is so ordered.

.....  
Judge.

[Endorsed]: ORIGINAL No. 1124 Civil IN  
THE United States District Court Southern District  
of California Southern Division THE CITIZENS NA-  
TIONAL BANK, Plaintiff vs. MARYLAND CAS-  
UALTY COMPANY, a corporation, Defendant STIP-  
ULATION WAIVING TRIAL BY JURY FILED  
JAN 9 1923 CHAS. N. WILLIAMS, Clerk By  
W. J. Tufts, Deputy HUNSAKER, BRITT & COS-  
GROVE, 1131-1143 TITLE INSURANCE BUILD-  
ING FIFTH AND SPRING STREETS LOS AN-  
GELES, CAL. Attorneys for PLAINTIFF

At a stated term, to-wit: The July, 1924, Term of the District Court of the United States of America, within and for the Southern Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, on Wednesday, the thirteenth day of August, in the year of our Lord one thousand nine hundred and twenty-four;

Present:

The Honorable Wm. P. James, District Judge.

The Citizens National Bank of )  
 Los Angeles, )  
 Plaintiff, )  
 )  
 vs. ) No. 1124 Civil.  
 )  
 Maryland Casualty Company, )  
 )  
 Defendant. )  
 )

Judgment is ordered to be entered upon findings of fact to be hereafter prepared by counsel, which shall



be in conformity with the conclusions expressed in the written opinion filed this day. The several motions of counsel made to the court at the conclusion of the hearing of the testimony, in so far as the same are not consistent with the decision as expressed in said opinion, are overruled, and an exception is allowed in each case in favor of the party adversely affected.

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES,) )	FINDINGS OF
Plaintiff, )	FACT AND
vs. )	CONCLUSIONS
MARYLAND CASUALTY )	OF LAW.
COMPANY, a Corporation, )	
Defendant. )	

This cause came on regularly for trial in the above entitled court on Thursday, the 20th day of December, 1923, at the hour of ten o'clock A. M. before the court, the Honorable William P. James, judge presiding, without a jury, a trial by jury having been duly waived in writing by the parties hereto and each of them, said parties appearing by counsel; pleadings having been filed raising issues of law and fact for the determination of the court and evidence oral and documentary having been offered and received by the court on behalf of the respective parties, and the hearing of said cause having proceeded from day to day with various continuances thereof until Friday,

the 11th day of January, 1924, at which time said court having heard all of the evidence offered by said parties and having heard arguments of counsel for the respective parties, and thereafter counsel for said parties having presented written briefs for the consideration of the court, and the court having duly considered all of said matters and being fully advised in the premises, finds the following facts, to-wit:

I,

That at all times between the 26th day of December, 1919, and the 3rd day of May, 1921, the plaintiff was, and now is, a banking association duly incorporated and existing under and by virtue of the laws of Congress of the United States of America, and having its principal place of business in the city of Los Angeles, state of California.

That at said times the defendant was, and now is, a corporation organized and existing under and by virtue of the laws of the state of Maryland, and duly authorized by the state of California to act as surety upon bonds and undertakings, including fidelity bonds of employees; and during all of said times was, and yet is, transacting business as such surety in said state of California.

That at all times between said dates California Cotton & Factorage Company was, and now is, a corporation duly organized and existing under and by virtue of the laws of the state of California, having its principal place of business at the city of Los Angeles in said state, and was engaged in the business

of buying, selling, handling and dealing in cotton and all the by-products thereof.

## II.

That one J. B. Sears was the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company during all of said time between said 26th day of December, A. D. 1919, and said 3rd day of May, 1921, save and excepting that between the 20th day of May, 1920, and the 9th day of September, 1920, said J. B. Sears ceased to act as secretary of said corporation, but during said time continued to act as manager of said company, and retained all the powers and privileges granted him under the by-laws as secretary to execute all proper instruments for and on behalf of said company, to sign the name of said company to checks, drafts, bills of exchange, receipts, acceptances or acquittances, and to endorse his name on checks, drafts, bills of exchange, notes and other evidences of indebtedness which would thereupon be valid and binding upon said corporation without any additional previous authorization or subsequent ratification by any of the officers of said corporation, and that during said time from said 20th day of May, 1920, until said 9th day of September, 1920, one C. H. Hartke acted as secretary of said corporation.

## III.

That on the 26th day of December, 1919, the defendant herein executed and delivered to the California Cotton & Factorage Company a certain fidelity bond



or policy of fidelity and guarantee insurance in the words and figures following, to-wit:

“Register No. 5493. (\$2.50 cancelled revenue stamps attached)

MARYLAND CASUALTY COMPANY  
BALTIMORE

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WHEREAS, J. B. Sears, hereinafter called the Employee, has been appointed to a position in the service of California Cotton & Factorage Co., Los Angeles, Cal. hereinafter called the Employer, and

WHEREAS, said Employee has been required to furnish Bond.

NOW, THEREFORE, in consideration of a certain premium to be paid annually in advance during the term of this bond, and of the Employer's written statements relative to the Employee, his duties and accounts, it is hereby agreed that the MARYLAND CASUALTY COMPANY, a corporation of Maryland, hereinafter called the Company, will, within two (2) months after the receipt of satisfactory proofs of loss, reimburse the Employer for any loss, not exceeding Fifty Thousand Dollars (\$50,000), of money, securities or other personal property (including that for which the Employer may be responsible to others), which the Employer shall have sustained by reason of any act or acts of FRAUD, DISHONESTY, FORGERY, EMBEZZLEMENT, WRONGFUL ABSTRACTION or WILFUL MISAPPLICATION on the part of the Employee, while in the perform-



ance of his duties as Secretary in the service of said Employer and, occurring during the continuance of this bond.

THIS BOND is executed upon the following express conditions: which are conditions precedent to the right of the Employer to recover hereunder:

1. That the term of this bond begins at noon on the 1st day of November A. D. 1919, and ends with (a) the permanent or temporary retirement of the Employee from the service of the Employer; (b) the discovery by the Employer of loss hereunder; or (c) the cancellation of this Bond by the Employer or the Company.

2. That all statements which the employer has furnished to the Company concerning the Employee or his duties or accounts are warranted by the Employer to be true; that the Employer has no knowledge of any act of fraud or dishonesty committed by the Employee while in the service of the Employer or elsewhere; that if the Employer become aware of the Employee committing any act of fraud or dishonesty, or of the Employee gambling or speculating or committing any disreputable, lewd or unlawful act, the Employer shall, within ten (10) days thereafter, notify the Company by registered letter, addressed to the Company at its Home Office, Baltimore, Maryland, and the Company shall not be liable for any loss subsequently incurred by the Employer through any act of the Employee unless the Company shall have consented, in writing, to continue its liability under this bond.

3. That any loss covered hereunder be discovered during the continuance of this bond or within six (6) months after its termination, and notice of such loss be sent by telegraph and by registered letter, both addressed to the Company at its Home Office, Baltimore, Maryland, within ten (10) days after the discovery; that an itemized statement of the loss shall be filed with the Company by the Employer within ninety (90) days after the date of said notice of loss; that if required by the Company, the Employer shall produce for investigation all books, vouchers, and evidence in the Employer's possession, and render every assistance (except pecuniary) capable of being rendered by the Employer, that may aid in bringing the Employee to justice.

4. That the Employer and the Company shall share any recovery (excluding insurance and reinsurance), made by either on account of any loss, in the proportion that the amount of the loss borne by each bears to the total amount of the loss.

5. That this bond may be terminated by the Company upon fifteen (15) days' notice in writing, to the Employer and likewise the Employer may terminate this bond by notice in writing to the Company, specifying the date of cancellation. Upon the termination of the bond and provided no loss has been reported, the Company shall refund the pro rata, unearned premium.

6. That should the employee become guilty of any criminal offense covered by this bond, the Employer shall immediately, on being requested by the

Company so to do, lay proper information before an officer or other body having authority to issue warrant for the arrest of the Employee, and verify the same as required by law, and furnish the Company every aid and assistance (not pecuniary) that can be rendered by the Employer his agents or servants, in the apprehension and prosecution of the Employee.

7. That should the Employer and the Company disagree regarding the amount of any claim made under this bond, the amount may, at the election of the Employer or the Company be determined by arbitrators; one to be selected by the Employer, one to be selected by the Company, and a third (in the event of failure to agree upon the amount of the claim) by the two so selected; the written decision of the majority of said arbitrators shall be binding and conclusive as to the amount of such claim and the total expense of such arbitration shall be paid by the Company.

8. That no action or proceeding shall be brought to recover any claim under this bond unless begun within twelve (12) months from the time detailed statement of loss shall have been given to the Company by the Employer, unless by statute of the state in which suit is brought agreements such as in this condition contained are expressly prohibited.

SIGNED, sealed and dated this 19th day of December, A. D. 1919.



Not valid unless countersigned by an authorized official or agent of the Company.

E. E. Holly

Assistant Secretary.

Jno. T. Stone

President.

(SEAL)

Countersigned at Philadelphia, Pennsylvania this 26th day of December, A. D, 1919.

Louis J. Farley  
attorney-in-fact"

Indorsed as follows:—"No. 134580 ENTERED LINE SHEET 5080 REGISTER R-410 MARYLAND CASUALTY COMPANY INDIVIDUAL BOND \$50,000 ON BEHALF OF J. B. Sears to California Cotton & Factorage Co. Los Angeles, Cal. Dated November 1st, 1919. For Transfers or Renewal, Apply to HASELTINE SMITH, FIRE, LIFE AND GENERAL INSURANCE, 326 Walnut St. Phila."

That on the 8th day of November, 1920, said California Cotton & Factorage Company paid to, and there was accepted by, said Maryland Casualty Company, defendant herein, the sum of Two Hundred Fifty Dollars (\$250.00), being the cash premium to be paid annually in advance during the term of said bond under the provisions thereof. That said bond and all the provisions thereof continued and remained in full force and effect, and said bond and all the provisions thereof were in full force and effect continuously from said 26th day of December, 1919, to and until said 3rd day of May, 1921.



## IV.

That on said 26th day of December, 1919, and prior and subsequent thereto, and up to and including the 3rd day of May, 1921, save and excepting the period from May 20, 1920, to September 9, 1920, as hereinbefore in Finding No. 2 found, said J. B. Sears was the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, and as such, and in his capacity of secretary, was authorized to, and did, act as the general manager of said California Cotton & Factorage Company, and upon its behalf, and as its act and deed was authorized to, and did, make and enter into contracts and agreements and other instruments in writing, sign and issue checks, drafts, notes and other obligations of said California Cotton & Factorage Company. As such secretary, said J. B. Sears, pursuant to the by-laws of said California Cotton & Factorage Company, had, enjoyed and exercised complete and unrestricted power and authority to enter into any contracts or agreements and perform any and all acts and things necessary in carrying out and fulfilling the purposes and business of said California Cotton & Factorage Company.

## V.

That subsequent to said 26th day of December, 1919, and prior to said 3rd day of May, 1921, and during the term of said bond, and beginning more particularly on or about the 19th day of November, 1920, and at various times and at irregular intervals thereafter up to the 25th day of April, 1921, the plaintiff herein, in due and regular course of business, received

eighty-seven (87) sight drafts drawn upon said California Cotton & Factorage Company by various persons, firms and corporations in the total amount of eighty-two thousand four hundred eighty-seven dollars and ninety-six cents (\$82,487.96); that attached to each of said eighty-seven (87) sight drafts was one or more warehouse receipts, each receipt covering one bale of cotton, and that there were attached to said eighty-seven (87) sight drafts so received a total of fourteen hundred and seventy-six (1476) warehouse receipts for fourteen hundred and seventy-six (1476) bales of cotton; that each warehouse receipt had been, at the time of its receipt by the plaintiff herein, endorsed in blank, and said receipts were, and each one was, negotiable and transferable by delivery. Immediately following the receipt of each of said drafts by the plaintiff herein, each of said drafts was accepted in writing by and on behalf of said California Cotton & Factorage Company by its secretary J. B. Sears, then acting within the scope of his authority and the course of his employment. That immediately following said several acceptances by said California Cotton & Factorage Company, as herein found, and relying entirely thereon and for no other reason, plaintiff herein remitted and paid to the person, firm or corporation presenting said drafts for acceptance and payment the amount or face value thereof, and thereafter carried upon its books and accounts as Bills Receivable all such drafts and acceptances so received and paid and all warehouse receipts attached thereto were held by plaintiff as collateral security for the payment by said

California Cotton & Factorage Company of said drafts and acceptances; that the total face value of said eighty-seven (87) drafts was the sum of eighty-two thousand four hundred eighty-seven dollars and ninety-six cents (\$82,487.96), which sum the plaintiff herein paid and advanced, as herein found, to the various persons, firms or corporations presenting the same.

## VI.

That at various times and irregular intervals between said 19th day of November, 1920, and said 25th day of April, 1921, and in most instances immediately following the acceptance of each of said sight drafts and the payment thereof, as hereinbefore found, said J. B. Sears, then and there acting within the scope of his authority and the course of his employment as secretary of said California Cotton & Factorage Company, upon behalf, in the name, and as the act and deed of said California Cotton & Factorage Company, with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating and willfully misapplying said warehouse receipts, the cotton represented thereby, and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained, of thereby causing a loss to said California Cotton & Factorage Company of money, securities and personal property, for which it would be, and has, become responsible to the plaintiff herein, said J. B. Sears applied to, and secured from the plaintiff the warehouse receipts then in its possession, held as collateral security for the payment of



said drafts and acceptances and obtained by it in the manner hereinbefore found. That at said time, and as a part of the same transaction, in acknowledgment of the delivery to him of said warehouse receipts, said J. B. Sears executed and delivered to the plaintiff herein certain written instruments then and there designated as trust receipts; that during all of the time between said 19th day of November, 1920, and said 25th day of April, 1921, said J. B. Sears executed and delivered to the plaintiff eighty-seven (87) of said trust receipts, which trust receipts, other than the number and date thereof, and the amount of warehouse receipts mentioned therein, were of the following tenor and effect:

"California Cotton & Factorage Co. No. 77  
Cotton

TRUST RECEIPT

Los Angeles, California, Nov. 19, 1920

Received in trust from the

The Citizens National Bank of Los Angeles Bank of  
Los Angeles documents, described below, the purpose  
being to secure delivery of the shipments and secure  
outbound documents therefor, which shall be returned  
to said bank in cancellation of this receipt.

B/L No.———No. B/C———Mark———

CALIFORNIA COTTON & FACTORAGE CO.

J. B. Sears Mgr.

Compress or Yard Receipts

25 B/C Attached.

Dft. 2675.25"



That said J. B. Sears at the time of receiving said warehouse receipts and executing and delivering said trust receipts, as herein found, and prior and subsequent thereto represented to the plaintiff, its officers and agents, that, in order to make and complete sales of the cotton covered by said warehouse receipts, it would be necessary to surrender said warehouse receipts to the persons, firms or corporation issuing the same and obtain possession of and deliver said cotton to the common carriers of freight over which shipments of said cotton would be made to the purchasers thereof, receiving in exchange therefor bills of lading of said common carriers; that upon any such exchange being made he, the said J. B. Sears, would immediately thereafter return said bills of lading to the plaintiff herein, and at such time take up the trust receipt or trust receipts given by him to the plaintiff at the time and in acknowledgment of the delivery to him of warehouse receipts covering cotton sold, as aforesaid. That in said manner, and pursuant to said fraudulent and dishonest plan and scheme, said J. B. Sears, at various times and irregular intervals, procured from the plaintiff herein between the said 19th day of November, 1920, and said 25th day of April, 1921, fourteen hundred and seventy-six (1476) warehouse receipts for fourteen hundred and seventy-six (1476) bales of cotton, and issued and delivered to the plaintiff, in acknowledgment thereof, eighty-seven (87) of said trust receipts.

VII.

That subsequent to said 19th day of November, 1920, and prior to said 3rd day of May, 1921, at various times and irregular intervals between said dates, said J. B. Sears, then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such within the scope of his authority and the course of his employment, without the knowledge of said California Cotton & Factorage Company, or any of its officers or agents other than said J. B. Sears, pursuant to said *fraudulent* and dishonest plan and scheme by him entertained as hereinbefore found, *fraudulently* and dishonestly converted, misappropriated and willfully misapplied ten hundred ninety-one (1091) of said fourteen hundred and seventy-six (1476) warehouse receipts and ten hundred ninety-one (1091) bales of cotton represented thereby in the manner following, that is to say: said J. B. Sears, having obtained said warehouse receipts in the manner and for the purpose hereinbefore found, sold said cotton covered by said receipts to various and divers purchasers of cotton throughout the United States; that thereupon said J. B. Sears surrendered said warehouse receipts, or caused said warehouse receipts to be surrendered to the persons, firms or corporations issuing the same, secured possession of and delivered said cotton, or caused possession and delivery of said cotton to be made to common carriers of freight at various points in the states of California and Arizona, for shipment and delivery to the purchasers thereof, and

received from said common carriers bills of lading for said shipments of cotton. That said J. B. Sears immediately thereafter, in violation of his duties as secretary of said California Cotton & Factorage Company, and in violation of his promises and representations to the plaintiff, and in violation of the terms of said trust receipts, delivered by him to the plaintiff, all as herein found, but pursuant to said fraudulent and dishonest plan and scheme found herein, attached said bills of lading, or caused said bills of lading to be attached, to sight drafts prepared by him or under his direction and drawn upon the purchasers of said cotton by the California Cotton & Factorage Company and in favor of the Citizens National Bank of Los Angeles, and thereupon presented, or caused to be presented, said sight drafts with bill of lading attached for approval, acceptance and the immediate issuance of credit thereon to an officer of said bank other than the officer from whom said J. B. Sears had obtained said warehouse receipts and to whom he had delivered said trust receipts as hereinbefore found, and represented to said officer or officers to whom said sight drafts and bills of lading were presented as herein found, that the cotton covered by said sight drafts and bills of lading was cotton belonging to said California Cotton & Factorage Company and willfully failed to disclose to said officer or officers the fact, as herein found, that said bank then held trust receipts of said California Cotton & Factorage Company given by said J. B. Sears under the circumstances and for the pur-



poses as hereinbefore found, covering the cotton described in said bills of lading attached to said sight drafts. That thereupon said J. B. Sears, having first secured the approval of said officer of said bank to said sight draft with bill of lading attached as herein found, deposited, or caused to be deposited, said sight drafts with bill of lading attached with a teller of said plaintiff bank, and received at that time from said teller and from said bank credit upon the account of said California Cotton & Factorage Company for the amount of said sight draft. That at the same time said J. B. Sears presented, or caused to be presented, to a teller of said bank the bank pass-book of said California Cotton & Factorage Company and there was entered therein by said teller as a deposit in said bank to the credit of the account of said California Cotton & Factorage Company an amount equal to the amount of said sight drafts; that said J. B. Sears immediately thereafter, pursuant to said fraudulent scheme hereinbefore found, falsified the books and accounts of said California Cotton & Factorage Company by entering, or causing to be entered therein, the various amounts of money received from the various sales of cotton made and carried out as herein found and the various amounts shown as having been deposited and the various credits entered, as herein found, upon the bank pass-book of said California Cotton & Factorage Company as moneys and funds belonging entirely without limitation of any kind to said California Cotton & Factorage Company; and then and there willfully failed to enter in said books



of said California Cotton & Factorage Company any entry or memorandum showing that said warehouse receipts had been secured as herein found, or that any trust receipts had been issued as herein found, or that said moneys and credits entered in said bank pass-book were received in the manner as herein found, and that at that time or thereafter willfully failed to make, or cause to be made, any other entry or memorandum indicating that said funds or moneys were charged with any trust, or were in any manner money or funds other than the absolute and unencumbered funds of said California Cotton & Factorage Company.

That during and following the transaction of said J. B. Sears, as herein found, said J. B. Sears frequently represented to said California Cotton & Factorage Company, its officers and directors, that said various sums of money and said credits entered upon said bank pass-book and books of account of said California Cotton & Factorage Company as herein found, were the funds and moneys of said California Cotton & Factorage Company made or accumulated by said J. B. Sears in the conduct of the affairs of said California Cotton & Factorage Company, and though well knowing of the disposition and sale of said warehouse receipts and cotton in the manner as herein found, said J. B. Sears, on inquiry made of him, represented to the plaintiff and its officers at various and divers times between said 19th day of November, 1920, and said 3rd day of May, 1921, that the said California Cotton & Factorage Company still retained and that

he, the said J. B. Sears, as secretary of said California Cotton & Factorage Company, still had in his custody in the vaults and files of said California Cotton & Factorage Company all and every the various warehouse receipts surrendered to him by said plaintiff, as hereinbefore found. That the California Cotton & Factorage Company and the Citizens National Bank of Los Angeles and the directors and officers of each of said corporations believed, acted upon and were deceived by said dishonest and fraudulent representations and statements of said J. B. Sears, as herein found.

That said ten hundred and ninety-one (1091) bales of cotton disposed of by said J. B. Sears in the manner as herein found were at the time of such fraudulent and dishonest conversion, misappropriation and willful misapplication, as herein found, of the reasonable value of sixty-five thousand five hundred and ninety-four dollars and sixty-two cents (\$60,594 62), which amount was credited to the account of said California Cotton & Factorage Company with the plaintiff herein, in the manner herein found.

#### VIII.

That subsequent to said 19th day of November, 1920, and prior to said 3rd day of May, 1921, and at various times and irregular intervals between said dates, pursuant to said fraudulent and dishonest plan and scheme hereinbefore found, and contemporaneous with the several fraudulent and dishonest conversions, misappropriations and willful misapplication of said warehouse receipts, the cotton represented thereby, the

bills of lading for the same, and the moneys and credits realized therefrom, and the false and fraudulent representations made and the deceit practiced by said J. B. Sears upon the California Cotton & Factorage Company and the plaintiff and their, and each of their, officers and directors, all as herein found, said J. B. Sears, continuing to act within the scope of his authority and the course of his employment as secretary of said California Cotton & Factorage Company, fraudulently and dishonestly converted, misappropriated and willfully misapplied the moneys and funds placed to the credit of said California Cotton & Factorage Company following the various dishonest and fraudulent sales of cotton and dispositions of warehouse receipts and bills of lading, all as herein found, by using said moneys and funds for the purpose of dealing and speculating in cotton in the name of said California Cotton and Factorage Company and conducting such dealings and speculations at a loss and paying said losses out of said moneys and funds and in the payment of claims and demands incurred by said J. B. Sears in said dealings and speculations in cotton.

That no part of said sum of sixty thousand five hundred and ninety-four dollars and sixty-two cents (\$60,594.62), or of any other moneys or funds was used by said J. B. Sears, or by any other person in the payment or satisfaction either in whole or in part of any one or more of said eighty-seven (87) drafts and acceptances of the California Cotton & Factorage Company held by the plaintiff, as herein found. That



upon the death of said J. B. Sears, there were delivered to the plaintiff herein three hundred eighty-five (385) of the fourteen hundred seventy-six (1476) warehouse receipts obtained by said J. B. Sears, as herein found, being warehouse receipts remaining at the time of his death in the hands of said J. B. Sears as secretary of said California Cotton & Factorage Company. That said three hundred eighty-five (385) warehouse receipts, together with the three hundred eighty-five (385) bales of cotton represented thereby, were at the time of their delivery by said plaintiff to said J. B. Sears, in the manner and for the purposes as herein found, of the reasonable value of twenty-one thousand eight hundred ninety-three dollars and thirty-four cents (21,893.34).

That, relying entirely upon said false and fraudulent representations of said J. B. Sears herein found, and said deceits by him practiced upon it and them, as herein found, said California Cotton & Factorage Company, its directors and officers, continued the business of the said California Cotton & Factorage Company, and consented to said J. B. Sears, subsequent to said 19th day of November, 1920, continuing to act as the secretary of said company and to continue to perform the acts and things necessary in carrying out the business of said California Cotton & Factorage Company, and to continue to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith, as herein found. That said California Cotton & Factorage Company, its directors and officers, would not have consented to con-



tinuing the business of said California Cotton & Factorage Company subsequent to the 19th day of November, 1920, neither would they have consented to said J. B. Sears continuing to act as secretary of said California Cotton & Factorage Company after said date, neither would they, subsequent to said date, have consented to said J. B. Sears conducting any dealings or speculations in cotton, nor in incurring any indebtedness, nor contracting any financial obligations upon its behalf had it, or any of its directors or officers other than said J. B. Sears, known of the frauds, deceits, dishonesties, wrongful conversions, misappropriations and willful misapplications, or any of them, being practiced upon them and upon said Citizens National Bank of Los Angeles by said J. B. Sears, all as found herein.

#### IX.

That due to, growing out of, and because of the fraud, dishonesty, wrongful abstraction and willful misapplication of said warehouse receipts, the cotton held thereunder, said bills of lading and the money, proceeds and credits realized from the sale and disposition thereof by said J. B. Sears as secretary of said California Cotton & Factorage Company in the manner herein found, said California Cotton & Factorage Company has sustained a loss and has become, and is, responsible to the plaintiff herein in the amount of sixty thousand five hundred and ninety-four dollars and sixty-two cents (\$60,594.62), with interest thereon at the rate of seven per cent. (7%) per annum from and after the 25th day of April, 1921.

X.

That following said fraudulent, dishonest, wrongful and willful misappropriations and misapplications by said J. B. Sears of the moneys, securities and personal property of said California Cotton & Factorage Company, as herein found, said California Cotton & Factorage Company immediately upon the discovery by it of the loss sustained and responsibility incurred, as herein found, and within ten (10) days after such discovery, notified said Maryland Casualty Company, defendant herein, at its home office at Baltimore, Maryland, by telegraph and by registered letter of such loss sustained and of such responsibility incurred as herein found, and within ninety (90) days after the date of said notice of loss filed with said Maryland Casualty Company at its home office at Baltimore, Maryland, an itemized statement of said loss sustained and said liability incurred, as herein found, and thereafter, and upon the request of said Maryland Casualty Company, produced for investigation all books, vouchers and evidence in the possession of said California Cotton & Factorage Company, and the same were thereafter investigated by said Maryland Casualty Company.

That said J. B. Sears shot himself on Saturday morning, the 30th day of April, 1921, and died from the effects thereof on Wednesday, the 3rd day of May, 1921.

That, notwithstanding the service of said notices upon the defendant herein by said California Cotton & Factorage Company, said defendant has failed and

refused, and still fails and refuses, to reimburse said California Cotton & Factorage Company for the loss it has sustained and responsibility to others it has incurred under the terms of said bond, by reason of the fraud, dishonesty, wrongful abstraction and willful misapplication on the part of said J. B. Sears while in the performance of his duties as secretary of said California Cotton & Factorage Company, as herein found.

#### XI.

That heretofore on the 9th day of May, 1922, the plaintiff herein obtained a judgment against said California Cotton & Factorage Company in the amount of ninety thousand two hundred eighty-one dollars and one cent (\$90,281.01) in the Superior Court of the State of California, in and for the county of Los Angeles, said judgment being entered in book 535 at page 30 of the records of judgments of said Los Angeles county, state of California; that said judgment was founded in part on drafts accepted by said California Cotton & Factorage Company and trust receipts substituted by said J. B. Sears for said warehouse receipts, as herein found.

#### XII.

That on the 1st day of September, 1921, California Cotton & Factorage Company by an instrument in writing assigned, transferred and set over to the plaintiff all its right, title or interest in and to that certain bond hereinbefore in finding No. 3 described and set forth at length, and in and to all moneys due or to



become due thereunder, including all claims, demands, causes of action, or choses in action, in every clause, article or things in said bond contained.

XIII.

It is not true that subsequent to said 26th day of December, 1919, and prior to the 3rd day of May, 1921, and at various times between said dates, and during the term of said bond and while the same was in full force and effect, said J. B. Sears, then and there the duly and regularly appointed, qualified and acting secretary of said California Cotton & Factorage Company, acting as such within the scope of his authority and in the course of his employment, without the knowledge of said California Cotton & Factorage Company or any of its officers or agents other than said J. B. Sears, fraudulently, dishonestly, wrongfully or willfully converted and applied five thousand five hundred and three dollars and eighty-eight cents (\$5,503.88), or any money whatsoever, of said California Cotton & Factorage Company to his own uses and purposes, or in satisfaction of his personal obligations, as alleged in the plaintiff's second cause of action.

XIV.

That it is provided in paragraph 7, subdivisions A and B, of a statement signed "California Cotton & Factorage Company, by T. J. West, Treasurer," which statement accompanied the application of said J. B. Sears for said bond, as follows:



- |                                                                                                                                                                                                                                                                                                                                                                                                                          |                                                                                                                                                                                               |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>7 (a) If applicant's duties embrace the custody of CASH, state LARGEST amount likely to be under his or her control at any one time.</p> <p>(b) For what length of time is applicant apt to have control of such amount?</p> <p>(c) Will applicant have control of securities?</p> <p>(d) If so, state value of same, whether negotiable, and if such securities are under joint control with some other officer.</p> | <p>(a) Cash be in bank.</p> <p>(b) No cash in personal control, only as checks may be issued or received for deposit.</p> <p>(c)</p> <p>(d) Negotiable all of them and under his control.</p> |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

That it is not true that said J. B. Sears, with the knowledge and consent of said California Cotton & Factorage Company and of its officers, other than said J. B. Sears, handled all or any of the cash of said California Cotton & Factorage Company for such use or purpose as said J. B. Sears deemed best, and it is not true that with the knowledge or consent of said California Cotton & Factorage Company, or any of its officers, other than said J. B. Sears, all or any of the cash of said corporation was handled by said J. B. Sears without being required to render an account for the same, or without being required by said California Cotton & Factorage Company, or its officers, to make an audit of all or any of said cash so handled, or without any process of bookkeeping, so as to furnish in-

formation to said defendant as to the disposition of the moneys of said California Cotton & Factorage Company. That said J. B. Sears kept in the safe of said California Cotton & Factorage Company funds of said company, in an amount never over fifty dollars, and used said funds to pay the petty expenses of the operation of said office, and that all other funds and receipts of said company were deposited in said bank.

XV.

That it is provided in said paragraph 8, subdivision A of said statement accompanying the application of said J. B. Sears, as hereinbefore found, as follows:

8	(a) Will applicant be authorized to pay out of the CASH in his or her custody any amount on your account?	(a) All things paid by check.
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(b) in what manner is such authority given?	(b) By-Laws.
---------------------------------------------	--------------

It is not true that, with the knowledge or consent of said California Cotton & Factorage Company, or its officers, the said J. B. Sears was permitted to use or did use the cash of said California Cotton & Factorage Company in such manner as he deemed best.

XVI.

That it is provided in paragraph 12 of said statement accompanying the application of said J. B. Sears, as hereinbefore found, as follows:

- 12 (a) At what intervals will applicants books, accounts, stock and securities be inspected and audited and verified with funds on hand or in bank? (a) At least once in BOOKS every CHECKED months. UP EACH MONTH
- (b) At what intervals and in what manner will outstanding accounts, as shown by applicant's books or reports, be verified? (b) At least once WE HAVE NO SUCH ACCOUNTS in every months.
- (c) If salesman or collector, how often do you bill the trade direct? (c)
- (d) By whom will above inspections and audits be made? (d) T. J. WEST, TREASURER official capacity.

That said T. J. West, treasurer of said California Cotton & Factorage Company, a cotton dealer of many years experience, visited the office of said California Cotton & Factorage Company semi-monthly during the term of said bond as herein found, and at such times conferred with said J. B. Sears respecting the business of said company and checked over the books of said company, but not in detail at any time, examining the cotton account, being the purchase and sales cotton accounts, showing the cotton bought and sold, and at said times examined the records disclosing the amount of cotton bought, the amount of cotton sold, the number of bales unsold, the entries respecting the hedging of the same, and also examined the cash account and

the acceptance account, together with the cotton tickets indicating the number of bales of cotton on hand, and compared the same and determined that they corresponded to the acceptances in the plaintiff bank; and at such times said T. J. West checked the books of said company for the purpose of determining the amount of money owing by said company to said Citizens National Bank, and examined the statements and books of said company to observe and did observe the amount of cotton purchased and the number of cotton tickets and bales of cotton on hand and examined the ledger books of said company and the various accounts therein, including the cotton account, and checked the same with the bookkeeper's statement furnished at the end of each month. That a report of the condition of the business of said California Cotton & Factorage Company was prepared by the bookkeeper of said company under the direction of said J. B. Sears on the first day of each month during the time covered by said bond as herein found. That said monthly reports were delivered to said J. B. Sears by said bookkeeper. That one copy of said monthly report was kept in the office of said California Cotton & Factorage Company and one copy thereof was shown monthly to the president of said corporation and examined by him. That said T. J. West checked the accounts of said company, including the bank account, semi-monthly by said statements rendered by the bookkeeper as herein found. That other than as herein found no audit was made of the books, accounts, stocks and securities of said



California Cotton & Factorage Company and no inspection, audit or verification of the funds on hand or in bank of said California Cotton & Factorage Company was made at any time by said company, or any of its officers. That it is not true that if an audit had been made each month, as provided in the contract between the California Cotton & Factorage Company and said defendant, it would have revealed the facts as herein found, and that the loss herein found to have been sustained could have been checked, lessened and stopped.

#### XVII.

That other than the notices sent by said California Cotton & Factorage Company to the defendant, as hereinbefore in finding No. X found, no notice, knowledge or information was furnished to defendant by said California Cotton & Factorage Company, or by the plaintiff herein. That until May 19th, 1921, no notice, knowledge or information concerning the same was furnished to the defendant by said California Cotton & Factorage Company, or by the plaintiff herein. That said California Cotton & Factorage Company, or the plaintiff herein, did not discover the loss occasioned to said California Cotton & Factorage Company by said acts of said J. B. Sears, as herein found, until the 19th day of May, 1921.

#### XVIII.

It is not true that the verbal notice to defendant of the loss of said California Cotton & Factorage Company, as herein found, was more than twenty-one days after the discovery of the loss sustained by said Cali-

fornia Cotton & Factorage Company, through the acts of said I. B. Sears, as herein found, but the court finds that the verbal notice to defendant of said loss was given on the day of the discovery of said loss by said California Cotton & Factorage Company.

XIX.

It is not true that all of the moneys of said California Cotton & Factorage Company handled by said J. B. Sears were used in or for the purchase of cotton or other commodities or on behalf of or which became the property of said California Cotton & Factorage Company, or for the purpose of paying the expense or cost of operation of said Californit Cotton & Factorage Company.

It is provided in said statement accompanying application of said J. B. Sears, as hereinbefore found, as follows:

It is agreed that the above answers are warranties and constitute the basis of and form a part of the consideration of the bond executed, or about to be executed, by the Maryland Casualty Company in favor of the undersigned, upon the person above named, and also all continuations or renewals thereof, or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by said company.

It is not true that the warranties in and by said statement signed, as hereinbefore found, were untrue or broken in all or any of the respects alleged in defendant's answer, and it is not true that defendant is

or has been released from all or any of the obligations for liability to plaintiff as herein found upon or under said bond.

## XX.

It is not true that the loss occurring to said California Cotton & Factorage Company, as herein found, was with full knowledge or with any knowledge of said California Cotton & Factorage Company, or any of its officers or agents, at the time of said loss, other than said J. B. Sears. It is true that said loss, as herein found, was with the full knowledge at the time of said loss of said J. B. Sears, and with the consent and due to the acts of said J. B. Sears. It is not true that said California Cotton & Factorage Company has breached any of the warranties of said bond or has done anything contrary to or in violation of the terms of said statement accompanying the application of said bond that produced or was the cause of the loss herein found to have been sustained by said California Cotton & Factorage Company, and it is not true that said loss as herein found to have been sustained by said California Cotton & Factorage Company would not have occurred had said California Cotton & Factorage Company observed the conditions of said bond and written statement.

## XXI.

The California Cotton & Factorage Company was organized under the laws of the state of California on or about August 12, 1919, with an authorized capital

of fifty thousand dollars (\$50,000.00), and that the officers thereof were as follows:

T. W. McDevitt, President;  
C. W. Hartke, Vice-President;  
J. B. Sears, Secretary;  
T. J. West, Treasurer,

and that said directors were as follows:

T. W. McDevitt;  
C. W. Hartke;  
J. B. Sears;  
T. J. West;  
J. P. Conduit;

that no stock was issued by said corporation until on or about January 29, 1920, when stock certificates were issued as follows:

496 shares to said T. J. West;  
1 share to said T. W. McDevitt;  
1 share to said J. P. Conduit;  
1 share to said J. B. Sears;  
1 share to said C. W. Hartke.

That on December 1, 1920, the said T. J. West sold his said 496 shares of stock to said J. B. Sears. That upon said 1st day of December, 1920, said T. J. West surrendered all of his stock certificates, and that the same were cancelled and new certificates for 496 shares dated May 24th, 1920, were delivered to the said J. B. Sears, who later in said month of December, 1920, delivered to said T. J. West, in consideration of the sale and surrender to him of said stock, a promissory note endorsed by said J. B. Sears, in the principal amount of twenty thousand dollars (\$20,000.00). That it was known to said California Cotton & Factorage Com-



pany and all its officers and agents that said T. J. West had sold and transferred his said stock to said J. B. Sears, and that said J. B. Sears was the manager and agent and in charge of the entire business affairs of said California Cotton & Factorage Company. but it was not known at said time by said officers, or any of them, that said business was being run at a loss. All of said officers of said California Cotton & Factorage Company, including said T. J. West, and excepting said J. B. Sears, believed and said T. J. West and the president of said California Cotton & Factorage Company had been informed by said J. B. Sears, that said business was being run at a profit.

That the officers of said California Cotton & Factorage Company on or about December 1, 1920, knew that the price of cotton was down; that debts and obligations to plaintiff herein and other corporations, partnerships and persons were being incurred, and that some of said debts were due and some of said obligations and indebtedness had been unpaid. It is not true that all or any of the acts or conduct of the affairs of said California Cotton & Factorage Company by said J. B. Sears herein found to have been fraudulently and dishonestly conducted by him were at all of the times or at any time prior to May 19, 1921, or known by said California Cotton & Factorage Company, or by any of its officers, other than said J. B. Sears, to have been dishonest and fraudulent as herein found.

That on and after December 1, 1920, said J. B. Sears became and was the practical owner of the entire assets and business of said California Cotton & Factorage Company, and that for all practical pur-

poses, on and after said last mentioned date, said California Cotton & Factorage Company became and was a corporation sole, to-wit, the said J. B. Sears, and that said corporation continued to act as a corporation sole, to-wit. said J. B. Sears, from and after December 1, 1920, until on or about May 3, 1921.

XXII.

It is not true that the defendant has requested, and that the California Cotton & Factorage Company has refused to produce its books, papers, documents, vouchers, minutes, by-laws, and correspondence for inspection. It is true that said documents upon the demand of the defendant herein were within a reasonable time after such demand produced for the inspection of and were inspected and audited by officers of said defendant. It is not true that the California Cotton & Factorage Company, or any of its officers or agents other than said J. B. Sears, had knowledge of any correspondence from the plaintiff herein respecting the amount of money due said plaintiff from said California Cotton & Factorage Company until on or about May 1, 1921, and it is not true that prior to the 19th day of May, 1921, the officers or agents of said California Cotton & Factorage Company, excepting said J. B. Sears, had any notice or knowledge or information of the fraudulent and dishonest acts of said J. B. Sears alleged in said complaint and herein found to be true.

XXIII.

It is true that said J. B. Sears was the general manager of said California Cotton & Factorage Com-

pany. It is not true that said Company had no meeting of its Board of Directors and it is not true that said company had no minutes of its meetings; and it is not true that the Board of Directors did not meet upon notice, or otherwise. It is not true that said company has no minutes of its meetings, and it is not true that said Board of Directors had no meetings. It is true that said J. B. Sears as the general manager and as the secretary of said California Cotton & Factorage Company, at all times had notice and knowledge of all acts and transactions by and between said California Cotton & Factorage Company and the plaintiff herein. It is not true that said California Cotton & Factorage Company failed or refused to carry out the terms or any of the terms of said bond herein found to have been given by the defendant herein.

#### XXIV.

That of the eighty-seven (87) sight drafts accepted by said J. B. Sears, between the 19th day of November, 1920, and the 25th day of April, 1921, in the manner and for the purposes as herein found, twenty-five (25) of said eighty-seven (87) sight drafts had been accepted by said J. B. Sears prior to December 1, 1920, which twenty-five (25) sight drafts are in the total amount of twenty-nine thousand three hundred thirty-seven dollars and ninety-nine cents (\$29,337.99).

That of the fourteen hundred and seventy-six (1476) warehouse receipts for fourteen hundred and seventy-six (1476) bales of cotton attached to said eighty-seven (87) sight drafts and delivered by the plaintiff to said J. B. Sears, in the manner and for the



purposes as herein found, four hundred and fifty-five (455) warehouse receipts for four hundred and fifty-five (455) bales of cotton were attached to said twenty-five (25) sight drafts accepted prior to December 1, 1921. That said four hundred and fifty-five (455) warehouse receipts, together with the four hundred and fifty-five (455) bales of cotton represented thereby, at the time of their delivery by said plaintiff to said J. B. Sears, as herein found, were of the reasonable value of twenty-nine thousand three hundred thirty-seven dollars and ninety-nine cents (\$29,337.99).

That of the eighty-seven (87) trust receipts delivered by said J. B. Sears to the plaintiff herein, between the 19th day of November, 1920, and the 25th day of April, 1921, in the manner and for the purposes as herein found, the first twenty-five (25) of said eighty-seven (87) trust receipts were executed and delivered by said J. B. Sears prior to December 1, 1920, which twenty-five (25) trust receipts covered said four hundred and fifty-five (455) warehouse receipts for said four hundred and fifty-five (455) bales of cotton.

That upon the death of said J. B. Sears, as herein found, said California Cotton & Factorage Company returned to the plaintiff herein seventy-six (76) of said four hundred and fifty-five (455) warehouse receipts for seventy-six (76) of said four hundred and fifty-five (455) bales of cotton delivered to said J. B. Sears as secretary of said California Cotton & Factorage Company prior to December 1, 1920, in the manner and for the purposes as herein found. That



at the time of their delivery by said plaintiff to said J. B. Sears, as herein found, said seventy-six (76) warehouse receipts and said seventy-six (76) bales of cotton represented thereby, were of the reasonable value of five thousand and fifty-six dollars and two cents (\$5,056.02).

### CONCLUSIONS OF LAW

From the foregoing facts the court concludes, as a matter of law:

1. That plaintiff is entitled to judgment against the defendant on the first cause of action herein in the amount of twenty-four thousand three hundred and twenty-one dollars and ninety-seven cents (\$24,321.97), with interest thereon at the rate of seven (7) per cent. per annum from the 15th day of October, 1921, and costs of suit incurred herein.

2. That the plaintiff is not entitled to judgment against the defendant in the second cause of action herein, and that the plaintiff take nothing against the defendant under said second cause of action.

3. That the plaintiff is entitled to its costs incurred herein.

Let judgment be entered accordingly.

Done in open court this 7 day of February, 1925.

Wm P James

Judge.

[Endorsed]: ORIGINAL No. 1124 Civ. IN THE United States District Court Southern District of California Southern Division The Citizens National Bank of Los Angeles. Plaintiff, vs. Maryland Casualty Company, a Corporation, Defendant. FINDINGS OF

FACT AND CONCLUSIONS OF LAW. Receipt of a copy of the within is hereby admitted this day of 25th Feb 1925 Bicksler Smith & Parke Attorney for Deft FILED MAR 7 1925 CHAS. N. WILLIAMS, Clerk By Edmund L. Smith Deputy Clerk HUNSAKER, BRITT & COSGROVE 1031-1044 Title Insurance Building Fifth and Spring Streets LOS ANGELES, CAL. Attorneys for.....

IN THE DISTRICT COURT OF THE UNITED  
STATES SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION

THE CITIZENS NATIONAL )  
BANK OF LOS ANGELES, )

Plaintiff, )

-vs-

MARYLAND CASUALTY )  
COMPANY, )

Defendant. )  
- - - - -

No. 1124 Civil  
: OBJECTIONS TO  
FINDINGS

The defendant objects to the Findings as proposed by plaintiff in the following particulars:

I.

That portion of Finding VII. contained between Lines 18 and 25, Page 13 also Finding IX. as contained on page 15, for the reason that the cotton company was obligated under its trust receipt to return to plaintiff's bank only the "out-bound documents" (that is, the price realized on re-sale) of the 1091

bales of cotton. The sum of \$60,594.62, as set forth in the portion of Findings objected to, was the original cost price of the cotton and not the re-sale price.

Defendant objects to that portion of Finding XXIV. contained on Lines 12 and 13 of page 27. for the reason that the value to be placed on the cotton tickets, so far as plaintiff bank is concerned, is the amount of the "out-bound Documents" (that is, the amount for which the cotton was sold). It must be admitted that if the "out-bound documents" (that is, re-sale price of the cotton) had been returned to the bank, the trust obligation would have been discharged. The trust receipt expressly provides that the return of the "out-bound documents" shall be in cancellation of the trust receipt.

For the same reason defendant objects to the Conclusion of Law I., page 28, for the reason that the amount therein specified is the purchase price of the cotton and not the amount of the "out-bound documents" (that is, re-sale price). (The auditor's report filed in the action indicates the face value of the out-bound documents (that is, re-sale price of the cotton tickets) which were not returned to the bank and the exact amount can be ascertained).

## II.

Defendant objects to and asks that all that portion of Finding VI. contained between Lines 17 to the words "as aforesaid" in Line 32, Page 9 be stricken;

Also that portion of Finding VII. contained on Lines 15 to 19, Page 11, and beginning with the words "and represented" on Line 15, and ending with

the words "Factorage Company" on Line 19, be stricken;

For the reason that the evidence shows that Sears made no representations in person or otherwise to any officer or officers of the plaintiff bank. All of the officers of plaintiff bank who testified, stated that at no time did Sears ever make any representations to them at the time he secured their approval for the deposit of the out-bound documents in the checking account and receiving a cash credit thereon.

III.

Defendant objects and asks that there be stricken from Finding VII. that portion beginning with the words "Falsified the books" on Line 8, page 12, and ending with the words "Factorage Company" on Line 16 of said page, for the reason that there is no evidence that any of the records of the corporation were falsified. The only evidence and the only contention of plaintiff was that there had been a failure to enter certain transactions in the books, which failure is particularly set forth in Finding VII.

IV.

Defendant objects to and asks that the following be stricken: that portion of Finding VI. commencing with the words "with the intent" on Line 7, Page 8 and ending with the words "plaintiff herein" on Line 14, for the reason that there is no evidence to show that Sears, when he obtained the cotton tickets from the bank, did so with any fraudulent or dishonest intent, but on the contrary the evidence shows, and particularly the letter of September eighth furnished



by the cotton company to the bank, that the substitution of trust receipts for cotton tickets was pursuant to a plan approved of both by the cotton company and by the bank; further, that such is the usual and customary way of handling such transactions; and further, Mr. McDevitt, president of the cotton company, testified that he knew that was being done and approved thereof. The letter of September eighth expressly provides for just such substitution. Mr. McDevitt testified that the only thing which Sears did that was not known to or approved of by the cotton company was his failure to return to the bank the "out-bound document" (that is, re-sale price of the cotton) directly in discharge of the trust receipts.

For the same reason defendant objects to and asks that that portion of Finding VII., beginning with the word "in" on Line 32, page 10, and ending with the word "plaintiff" on Line 3, page 11, be stricken. It must be admitted that the taking of the cotton tickets and substitution of trust receipts was not in violation of Sears' duties as secretary or in violation of any promise or representation made to the bank.

V.

Defendant objects to and asks that the words "Citizens National Bank of Los Angeles," as appearing upon Line 14 of page 13 be stricken, for the reason that there is no evidence that any dishonest representations were made to the plaintiff bank by Sears upon which the plaintiff bank extended any credit or loaned any moneys.

VI.

Defendant objects to and asks that there be stricken the following: that portion of Finding VIII. commencing with the words "and contemporaneous" Line 30, Page 13 and ending with the words "warehouse receipt" on Line 32, for the reason that there is no evidence to show that there was any misapplication or conversion of the warehouse receipts (that is, cotton tickets) but only of the proceeds from the re-sale of the cotton. Again it is urged that the securing of the cotton tickets and substitution of trust receipts and the re-sale of the cotton was strictly pursuant to the plan of operations approved of by both the cotton company and the bank. The only irregularity which the court's opinion indicates was tainted with dishonesty or fraud was the failure to return the re-sale price to the bank.

VII.

Defendant objects to that portion of Finding VIII. beginning with the words "Fraudulently and" on Line 8, Page 14 and ending with the words "cotton" on Line 18, for the reason that the evidence clearly discloses that there was not any conversion or misappropriation or misapplication by Sears of any funds insofar as the cotton company was concerned, but that the only misapplication was as to the plaintiff bank in that Sears, as secretary of the cotton company, handled certain property which was impressed with a trust in favor of the plaintiff bank, and he failed to discharge that trust insofar as the bank was concerned. No act of Sears was a violation of any duty

to the cotton company. A reference to the opinion of the trial court would indicate that the basis of the defendant's liability in this case is a breach of faith to the plaintiff bank, resulting from the failure of Sears, as secretary of the cotton company, to return the proceeds from the re-sale of the cotton, as provided in the trust receipts.

If the portion of said Finding so objected to is to remain, it should be made clear that the dealing and speculating in cotton, through which the money of the cotton company was lost, was carried on and was the act of the company and not the act of Sears individually. A fair inference may be drawn from the Finding as it now stands that the speculating was by Sears on his own account. All of the evidence of the case shows that the business of the cotton company was speculating in cotton, that is, buying and selling cotton. It had carried on this business for more than a year prior to November 19th, 1920, and the continuance of the business thereafter by Sears as a general manager and secretary of the company was not a breach of any duty. We respectfully submit that this Finding is wholly misleading and not supported by the evidence.

For the same reasons, defendant objects to and asks that that portion of Finding X., commencing with Line 1 Page 16 and ending with the word "found" on Line 5, be stricken.

Also, defendant objects to and asks to strike from Finding X. that portion contained in Lines 21, 22 and



23 Page 16 for the reason that the same is immaterial and has no place in the Findings.

VIII.

Defendant objects to and asks to strike from Finding XI. the following portion contained on Lines 13 and 14 as follows: "trust receipts substituted by said J. B. Sears for said warehouse receipts as herein found," because same is not the fact. The action in the Superior Court was based solely upon the drafts accepted by the cotton company.

IX.

Defendant objects to and asks that there be stricken from Finding XVI. that portion on Line 26 Page 20 "and also examine the cash account," also that portion of Lines 29 and 30 as follows: "and compared the same and determined that they corresponded to the acceptances in the plaintiff bank", also the following on Lines 15 and 16 on Page 21, "including the bank account"; all for the reason that the evidence shows that West at no time ever checked the cash account or checked the cotton on hand with the acceptances held by the plaintiff bank.

X.

Defendant objects to and moves to strike the word "not" on Line 23 of page 22, for the reason that it is true all of the moneys of the California Cotton & Factorage Company handled by Sears were used for the purchase of cotton or other commodities or for the purpose of paying the expenses or operation of the cotton company. At no time was it ever urged that any of the money belonging to the cotton company



was ever used for any purpose other than in the operation of the cotton company's business, save and except the moneys referred to in the second cause of action, being the overdraft by Sears.

Defendant asks that the following additional Findings be inserted:

I.

That there be inserted between Lines 12 and 13, on page 24 of the proposed Findings, the following:

That the four shares issued to T. W. McDevitt, John B. Conduit, J. B. Sears and C. W. Hartge were solely for the purpose of qualifying them as officers and that for all practical purposes and in fact the California Cotton & Factorage Company was from the date of its incorporation until December first, 1920, a corporation sole, to-wit the said T. J. West.

II.

Defendant requests that the following Finding be inserted at the end of Paragraph IV. and as Finding IVa.:

That on September 8th, 1919, and prior to the date when the California Cotton & Factorage Company began operations, it arranged with plaintiff a line of credit, up to the amount of \$200,000.00, which credit was to be protected in the manner outlined to it by letter dated September 8th, 1919, written to the plaintiff bank by the California Cotton & Factorage Company through J. B. Sears, its secretary. The contents of said letter of September 8th, 1919, and the manner of handling cotton purchases and sales through the plaintiff bank by the California Cotton & Factorage

Company, as outlined in said letter, was known to and approved of by the president and other officers of the California Cotton & Factorage Company and was an approved and customary method of handling the purchase and sale of cotton. That said letter of September 8th, 1919, among other things, stated:

“The financing of the cotton bought and sold will at all times be protected by collateral either in the form of warehouse receipts or railroad Bills of Lading which will be held by the bank as security, together with actual daily balances. These warehouse receipts or Bills of Lading will at times have to be replaced with trust receipts in order to facilitate the movement of the cotton, for example in making shipments from the different interior points, it is necessary to have the warehouse receipts in order to secure the cotton and get Bills of Lading for shipments and at such times trust receipts will be issued by ourselves until we can secure the out-bound Bills of Lading, after which times Bills of Lading attached to sight drafts are returned to the bank and the trust receipts taken up.”

That pursuant to said arrangement made with plaintiff bank, the California Cotton & Factorage Company did, during the cotton season of 1919-1920, cause drafts to be drawn upon itself covering cotton purchased by it, all of which drafts were accepted by the California Cotton & Factorage Company and paid by the plaintiff in the aggregate sum of \$1,172,217.96, all of which drafts so paid by the plaintiff were in turn repaid to plaintiff by the California Cotton & Factorage Company; that during the cotton season of 1920-

1921 and prior to the third day of May, 1921, there were drawn upon the California Cotton & Factorage Company drafts covering cotton purchased by it in the sum of \$233,150.69, all of which were accepted by the California Cotton & Factorage Company and paid by the plaintiff, and all of said drafts were in turn repaid to the plaintiff by the California Cotton & Factorage Company, save and except eighty-seven (87) drafts of the face value of \$82,487.96.

That the average costs per bale to the California Cotton & Factorage Company of cotton purchased during the 1919-1920 season was \$203.26 and the average price per bale for which it was sold was \$216.54. That about October, 1920, the beginning of the 1920-1921 cotton season, the cotton market began to decline, which decline continued up to on or about May 3rd. 1921. That the average cost per bale to the California Cotton & Factorage Company of cotton purchased by it through plaintiff bank during the 1920-1921 season was \$84.47 and the average price per bale for which it was sold was \$76.94 per bale.

### III.

Defendant requests that the following Finding be inserted:

"That save and except for moneys withdrawn by Sears, as set forth in plaintiff's second cause of action, the said J. B. Sears did not use or convert to his own use or benefit, or to the use and benefit of any person, firm or corporation, other than the California Cotton & Factorage Company, any of the money, funds or property of said California Cotton & Factorage Com-



pany, or any of the moneys, funds or property received from or belonging to the plaintiff."

Respectfully submitted,

Bicksler, Smith & Parke.

Attorneys for Defendant.

[Endorsed]: Original No. 1124 Civil IN THE United States District Court In and for the Southern District of California, SOUTHERN DIVISION In the Matter of THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, -vs- MARYLAND CASUALTY COMPANY, Defendant OBJECTIONS TO FINDINGS Received copy of the within Objections this 2nd day of March 2 1925 Hunsaker, Britt & Cosgrove Attorneys for Plaintiff FILED MAR 7 1925 CHAS. N. WILLIAMS, Clerk By Edmund L Smith Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts. Los Angeles, Cal. Telephone Trinity 4331 Attorneys for Defendant



IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

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THE CITIZENS NATIONAL BANK)	
OF LOS ANGELES, a corporation, )	
	)
Plaintiff, )	
	)
vs. )	JUDGMENT
	)
MARYLAND CASUALTY COM- )	
PANY, a corporation, )	
	)
Defendant. )	
	)
	)

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This cause came on regularly for trial in the above entitled court on Thursday the 20th day of December, 1923, at the hour of ten o'clock A. M. before the court, the Honorable William P. James, Judge, presiding, without a jury, a trial by jury having been duly waived in writing by the parties hereto; said parties appearing by counsel. Upon said trial evidence, oral and documentary, respecting the issues raised by the pleadings in the action was produced on behalf of the parties respectively, and received by the court; the evidence being closed, the arguments of the counsel for the parties having been heard, the cause was submitted to the court for consideration and decision, and after due deliberation the court made and signed its special findings of fact and conclusions of law thereon,

the same being filed herein. and ordered judgment for the plaintiff in accordance therewith;

WHEREFORE, by reason of the law and the findings aforesaid, it is now by the court ORDERED, ADJUDGED AND DECREED that the said plaintiff, The Citizens National Bank of Los Angeles, a corporation, have and recover of and from said defendant, Maryland Casualty Company, a corporation, the sum of twenty-four thousand three hundred twenty-one dollars and ninety-seven cents (\$24,321.97), together with interest thereon at the rate of seven per cent (7%) per annum from the 15th day of October, 1921, in the sum of five thousand seven hundred seventy-nine dollars and seventeen cents (\$5779.17), and amounting in all at this time to the sum of thirty thousand one hundred one dollars and fourteen cents (\$30,101.14); and that said plaintiff also have and recover of and from the said defendant the costs of this action incurred by it, the said plaintiff, taxed at the further sum of Four hundred sixty one dollars and 30/100 (\$461.30/100), and that execution issue thereon.

JUDGMENT ENTERED This 9th day of March, 1925.

CHAS. N. WILLIAMS, CLERK,  
By Murray E Wire  
Deputy Clerk.

Service of copy of the foregoing judgment is hereby admitted this 7 day of March, 1925, and the same is hereby approved as to form as provided in Rule 45 of the rules of the United States District Court for the Southern District of California, Southern Division.

Bicksler, Smith & Parke,  
Attorneys for Defendant.

[Endorsed]: No. 1124 Civil IN THE District Court of Appeal Second Appellate District State of California THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, Defendant. JUDGMENT FILED MAR 7 1925 CHAS. N. WILLIAMS, Clerk By Murray E Wire Deputy Clerk HUNSAKER, BRITT & COSGROVE 1131-1143 Title Insurance Building Fifth and Spring Streets Los Angeles, Cal. Attorneys for Plaintiff.

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IN THE DISTRICT COURT OF THE UNITED STATES, SOUTHERN DISTRICT OF CALIFORNIA, SOUTHERN DIVISION.

. . . . .

THE CITIZENS NATIONAL	)	No. 1124 Civil.
	)	
BANK OF LOS ANGELES,	)	
	)	
Plaintiff,	)	
	)	OPINION.
vs.	)	
	)	
MARYLAND CASUALTY COM-	)	
PANY,	)	
Defendant.	)	

Hunsaker, Britt & Cosgrove: Attorneys for Plaintiff.

Bicksler, Smith & Parke: Attorneys for Defendant.

. . . . .

This action is brought by the plaintiff as the assignee of the California Cotton & Factorage Co. (a California corporation) which for brevity will be here-

inafter referred to as the cotton company, to recover on an undertaking given by the defendant to insure the cotton company against loss sustained by reason of unauthorized acts of J. B. Sears, who was secretary of said company. The cotton company was organized in September, 1919; during all of the times that will be mentioned, up to about September 1, 1920, T. J. West held 496 shares of the issued shares, and there were issued to T. W. McDevitt, John P. Conduit, C. H. Hartke and J. B. Sears one share each.

It may be first stated that the cotton company was, from the date of its organization and until West transferred his interest therein, a business medium only used primarily for the benefit of West. West and Sears were experienced cotton brokers. West was conducting a cotton brokerage business at Calexico, California, and Sears had come to Los Angeles after having been connected for a number of years with a large cotton brokerage concern in the south. West expected to and did devote his main energies to his business at Calexico, where he resided, which place was at the center of the cotton growing country of Southern California and Northern Mexico. Desiring to establish a Los Angeles cotton brokerage house, West and Sears, with the active assistance of McDevitt, organized the cotton company. West paid into the treasury of the company all of the money that was contributed in exchange for stock. There was some intimation that some others of the persons named as stockholders had contributed money or services, but as to whether that was the fact is doubtful. At any rate, it was quite clearly made to appear that the issu-



ance of stock to all persons except West and Sears was for the particular purpose of qualifying them to act as directors. The stock certificates for one share each to McDevitt, Conduit and Hartke, remained undetached from the stock book, and so remained at the time of the trial. At the organization meeting of the board of directors, McDevitt was elected president, and Sears secretary. Under the by-laws, as adopted by the corporation, the secretary was also the general manager. As showing that the cotton company's business was intended by West to be under the control of Sears, the by-laws provided that the secretary should be the general manager of the company and expressly limited the power of the president by the statement that the president should have such general power as was "not in conflict with the special authority given the general manager." The special authority conferred upon the secretary as general manager was of the widest scope; in that regard, the by-laws declared that:

"The secretary of this corporation shall also be the general manager and any and all contracts made, agreements entered into or instruments signed, checks or drafts issued, notes or any obligations signed or created by him as such general manager shall be valid and binding upon the corporation without the previous authorization or subsequent ratification of the president or any other officer or member of the corporation, and said general manager is hereby given complete and unrestricted power and authority to enter into any contracts or agreements and perform any

and all acts and things necessary and in line with the carrying out and fulfilling of the purposes of this corporation and connected with his duties as the general manager thereof, in the performance of which duties his authority is absolute and unrestricted."

Under the plan of organization as outlined, the cotton company opened its office in the City of Los Angeles, and proceeded to do business with Sears in charge. On the 28th of November, 1919, West made application to the defendant Casualty Company for a fidelity bond to run in favor of the cotton company to protect it against loss by reason of such misconduct of Sears as was particularly specified on the bond which was later issued. In that application, and responding to a schedule of questions to which the casualty company required answer to be made, West set forth that Sears was employed as secretary and manager at a minimum salary of \$5,000.00 per year, his total compensation being fixed on a basis of twenty-five per cent of the profits; he set forth that all checks received would be negotiable and under Sears' control; that Sears was authorized to sign checks on behalf of the cotton company; that no countersignature would be required, this statement of West having added to it, "the owners live in other cities". In answer to the company's interrogatory, "At what intervals will applicant's books, accounts, stock and securities be inspected and audited and verified showing funds on hand or in bank?" West's answer was, "Books checked up each month". The bond was issued by the defendant com-

pany on the 19th of December, 1919; it insured the company against loss in the maximum amount of \$50,000.00 occasioned by misconduct of Sears, as secretary; reciting that the company would "within two months after the receipt of satisfactory proofs of loss, reimburse the employer for any loss, not exceeding fifty thousand dollars (\$50,000.00) of money, securities or other personal property (including that for which the employer may be responsible to others) which the employer shall have sustained by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication on the part of the employee, while in the performance of his duties as secretary."

The bond contained the further statement that the representations which the employer had furnished to the company "concerning the employee or his duties or acts, are warranted by the employer to be true. . . . that if the employer became aware of the employee committing any act of fraud or dishonesty. . . . the employer shall, within ten days thereafter, notify the company. . . . and the company shall not be liable for any loss subsequently incurred by the employer through any act of the employee, unless the company shall have consented, in writing, to continue its liability under this bond."

The cotton season of 1919 ended about May, 1920. During that year, Sears, as manager of the company, bought and sold a large quantity of cotton, financed growers at different points, and his transactions exceeded considerably a million dollars. On the pur-



chase and sale of cotton for that year, his books showed a considerable profit. Because of advances made to cotton growers, which were not fully returned, however, an actual operating loss for that year resulted. The cotton year of 1920 and '21 was concededly a bad one. Sears during that year continued his operations in his usual way; however, his purchase and sales account showed a loss in a large amount. In order to secure funds, with which to carry on his operations, he failed to keep the agreement of the company with the Citizens National Bank for the return to the bank of securities designed to protect the loan account. By May of 1921 the company was hopelessly involved and owed the bank a sum considerably in excess of fifty thousand dollars, which was wholly unsecured. Toward the last of April, the bank began to check up on the loan account of the cotton company, and made an inquiry of McDevitt, who was the nominal president, and who had introduced Sears to the bank. McDevitt in turn went to Sears, and Sears admitted that he had used cotton ticket securities which he should have left with the bank to protect the loans. McDevitt had no notice of this condition previous to that time, and requested Sears to meet him at the bank on the following day, so that they might discuss the condition of affairs in which the cotton company found itself. On the following morning, McDevitt received word from Sears' house that the latter had committed suicide.

The books were then checked up, losses ascertained, and notice given to the defendant bonding company.



Other details than this are necessary to be stated in order that the questions involved may be discussed, but first of all it is proper to observe that this action must be considered having in view only the obligations created by the bonding company toward the cotton company, and strictly as though there had been no assignment. The plaintiff bank received its assignment long after Sears' death. In the resolution authorizing the assignment to be made the consideration was recited to be "that the said Citizens National Bank shall present and prosecute the claim of the California Cotton & Factorage Company arising under said bond and shall apply any and all moneys collected by it under or pursuant to the terms of said bond over and above the expense of collecting the same, to a reduction of the indebtedness of this corporation to said Citizens National Bank, *nor* or hereafter existing."

It is essential that this condition which shows the plaintiff bank to be a mere assignee for collection, be kept in mind, particularly as affecting that evidence offered to show that West transferred his stock (except one share) to Sears in the latter part of the year 1920.

It is the claim of the defendant that it owes nothing under the obligation of its bond for several reasons: (1) That it is not shown that Sears committed any act constituting a breach of duty against which the bond furnished indemnity; (2) That West represented that the books would be checked up at least once every month, which he did not do, thereby failing to discover the true condition of the business; (3) That the bond was exonerated at the date when West transferred his interest in the corporation to Sears.

At the time of his death, Sears was shown to have overdrawn his personal account with the cotton company in the amount of about fifty-five hundred dollars. The majority of the checks drawn, which the accountants have scheduled as a part of the overdraft, were drawn during the year 1920. Some are dated as of each month of the year. There are several checks drawn in 1921. This overdraft account is to be considered as being clear of some of the questions which affect the other shortage arising from unreturned securities. Of course, if Sears as general manager had no authority to overdraw his account with the company, then his act in using its money without permission would at least amount to a "misapplication" within the terms of the bond. From the representations made by West to the bonding company, it must be assumed that while Sears was permitted to draw the amount of five hundred dollars each month on salary account, he would not be authorized until the close of the cotton year, when profits could be ascertained, to collect anything additional based upon the understanding that he was to have twenty-five per cent of such profits. And yet it is not at all to be deduced from the evidence that West as the auditing officer and owner of the cotton company could not at any of the monthly checking periods have ascertained from the check book or other records in the office of his company that Sears was improperly drawing on the funds. West testified that his investigation of the books only went so far as to give him information as to the purchase and sales account—that is, how much cotton Sears was buying, how much he was selling,

and as to whether he was "hedging" his business. The latter term refers to a practice of brokers to give selling orders to protect against a decline of the market. It was admitted by witnesses familiar with that practice, however, that in the presence of a very unstable market, hedging would not prevent a loss occurring. Under the representation made by West that he would check the books every month, it became the cotton company's duty not only to report promptly to the bonding company any dereliction of Sears, in the regards specified in the bond, but upon the occurring of any such dereliction which West would have discovered had he made the inspection of the books and accounts which he agreed to make, the failure to make such inspection and report would exonerate the insurer; and it must be concluded that if the bonding company might in any event be held responsible for the overdraft of Sears on his personal account, that the cotton company relieved the insurer because it failed in its duty to properly inspect the accounts and make report.

Considering next the evidence as to the transfer of West's stock to Sears, and its effect upon the liability of the defendant: Remembering that, as has been already observed, the questions here are to be considered as though the cotton company was the plaintiff, the evidence of West, who was the owner of the cotton company, as to when he transferred his interest to Sears, must be allowed full weight. A different consideration might arise, were this an action by a creditor to enforce a stockholder's liability for cor-



porate debts against West. If West, being the company, declares to the defendant: "This corporation went under the ownership of Sears at a certain date, and Sears then came into full and complete control" he would announce such a change in the conditions as to make the hazard different from that existing when the insurer made its bond. Furthermore, public policy would not favor the enforcement of a contract which would permit an individual to indemnify himself against his own misconduct.

West testified that he made the sale of his stock to Sears during the latter part of August. He contended also that it was a part of the agreement of sale that the transfer should be considered as relating back to the month of May, 1920, but I think, the evidence on the subject being considered altogether, the best conclusion that can be made is to fix the date of the transfer at the first of September, 1920. We then must consider that from that date West owned no further interest in the business, and that Sears then became the sole proprietor of it. Therefore, if there exists any liability on the part of the insurer under the bond sued upon, it must be such only as accrued prior to the first of September, 1920.

Having disposed of the matter of the claim arising by reason of the overdrawing of the personal account of Sears, there is next to be considered the matter of the appropriation by Sears of certain securities which the plaintiff bank was entitled to hold as a pledge against the loan account of the cotton company. The bank had allowed to the cotton company, shortly after its organization, a line of credit up to the amount of



\$200,000.00, which was to be protected in the manner outlined to it by Sears in a letter dated September 8, 1919. In that letter Sears stated, and the conditions expressed were the ones upon which the bank concluded its loan arrangement, that:

“The financing of the cotton bought or sold will at all times be protected by collateral either in the form of Warehouse Receipts or Railroad Bills of Lading, which will be held by the Bank as security together with actual daily balances. These Warehouse Receipts or Bills of Lading will at times have to be replaced with Trust Receipts, in order to facilitate the movement of the cotton, for example in making shipments from the different interior points it is necessary to have the Warehouse Receipts in order to secure the cotton and get Bills of Lading for shipments and at such times Trust Receipts will be issued by ourselves until we can secure the Outbound Bills of Lading, after which times Bills of Lading attached to Sight Drafts are returned to the Bank and the Trust Receipts taken up.”

Briefly, under the plan referred to, when Sears as manager of the cotton company would buy cotton the seller would draw on the cotton company for the amount of the purchase price. Upon the draft being accepted by Sears for the cotton company, it would be transmitted to the loan department of the plaintiff bank, which would advance the money and receive as collateral the warehouse or storage tickets, covering the cotton concerned in the particular transaction.

When Sears desired to make a sale of the same cotton, it was necessary that he have possession of the warehouse ticket in order to make delivery. The arrangement with the bank permitted him to take out the warehouse ticket and substitute a trust receipt which was to evidence the right of the bank to have returned to it in lieu of cotton receipts the outbound bill of lading which would authorize it to make collection of the sale price and credit same to the loan account. The intention was, therefore, that the bank should at all times have its loan account protected by either warehouse receipts, or bills of lading and drafts on purchasers. The ordinary account books or records of the cotton company would not show a mishandling of the bank's securities.

When the cotton market became disturbed and the business as conducted by Sears began to show a loss on purchases and sales, Sears failed in his duty to the bank. After withdrawing cotton tickets or warehouse receipts, and carrying through his sale of the particular cotton, he, in a great many instances, numbering well toward one hundred, failed to replace the withdrawn tickets by outbound documents, which resulted in the end, in the bank being left with a debt of approximately \$80,000.00 owing to it by the cotton company, which was not secured by collateral as the agreement contemplated. The act of Sears was more than a breach of faith; it approached an embezzlement of collateral in which the bank held a qualified property interest. It is argued on behalf of the defendant that the bad conduct of Sears in this regard caused no loss to the cotton company, against which only the indem-

nity had been furnished; that the misuse of the collateral did not cause the cotton company to lose what it already owed to the bank. And, furthermore, that whatever criticism might be made of the conduct of Sears, that all of the proceeds which he received were devoted to the business of the cotton company and not appropriated by the manager to his own or any other person's use. To my mind, that argument draws too narrow a line in the interpretation of the terms of the bond. The cotton company contemplated that its loan account would at all times be protected by collateral received in the usual and ordinary course of its dealings. The securities of the kind first described, when once they reached the bank, if removed under the shifting arrangement referred to, were property for which the cotton company was responsible and was bound to return in their resulting equivalent to the bank. The bank was entitled to demand and recover from the cotton company the agreed equivalent of the cotton tickets had the equivalent at any time been found in possession of the latter. The unauthorized use of the securities by Sears should be held to amount to a wilful misapplication of property for which the cotton company was responsible to the bank. Sears' breach of faith did result in a loss to the cotton company, because it would add to its liabilities the value of the collateral illegally withheld by Sears and used without authority in the business.

My conclusion is that plaintiff is entitled to recover, but that its recovery must be limited to the face value of such cotton tickets as were withheld and not replaced by Sears prior to September 1, 1920. I have not segregated the amount but counsel will no doubt



be able to agree upon the sum of it. If not, I will make the calculation. Interest from the date of the demand made upon defendant is to be added.

Dated August 12, 1924.

Wm P James

District Judge.

[Endorsed]: No. 1124 Civil. U. S. DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA. THE CITIZENS NATIONAL BANK OF LOS ANGELES vs. MARYLAND CASUALTY COMPANY OPINION. FILED AUG 13 1924 CHAS. N. WILLIAMS, Clerk Louis J. Somers Deputy.

IN THE DISTRICT COURT OF THE UNITED STATES, SOUTHERN DISTRICT OF CALIFORNIA, SOUTHERN DIVISION.

.....  
THE CITIZENS NATIONAL ) No. 1124 Civil.  
BANK OF LOS ANGELES, )  
Plaintiff, ) MEMORANDUM  
vs. ) SUPPLEMENTAL  
MARYLAND CASUALTY ) TO OPINION  
COMPANY, ) FILED.  
Defendant. )

Hunsaker, Britt & Cosgrove: Attorneys for Plaintiff.

Bicksler, Smith & Parke: Attorneys for Defendant.

.....  
Counsel for the plaintiff has suggested that under the evidence heard in this case the date of the transfer of



the stock of West to Sears should be fixed at the 1st of December, rather than September 1st, as determined in the opinion heretofore filed. There was not available in the files, at the time the decision was made, a transcript of the testimony. In determining the date of the transfer of Sears' stock, I relied upon my notes taken principally of *Sears'* testimony. By comparison with extracts from testimony of other witnesses, which counsel has now particularly called attention to, I think that it is true that the incident referred to by West, wherein his negotiations for the sale of his stock were brought to a conclusion, did occur about the first of December, and that *Sears* misplaced the date. The statement in the opinion fixing the date of transfer as of the 1st of September, 1920, may therefore be considered as amended to read "December first, 1920".

Dated this 28 day of November, 1924.

Wm P James

District Judge.

[Endorsed]: No. 1124 Civil. U. S. DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA, SOUTHERN DIVISION. THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, Defendant. MEMORANDUM SUPPLEMENTAL TO OPINION FILED. FILED NOV 28 1924 CHAS. N. WILLIAMS, Clerk Murray E Wire Deputy

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

.....

THE CITIZENS NATIONAL )	No. 1124 Civil.
BANK OF LOS ANGELES, )	:
Plaintiff, )	:
vs. )	: MEMORANDUM
MARYLAND CASUALTY )	: SUPPLEMENTAL
COMPANY, )	: OPINION.
Defendant. )	

Hunsaker, Britt & Cosgrove: Attorneys for Plaintiff.  
Bicksler, Smith & Parke: Attorneys for Defendant.

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Subsequent to the supplementary memorandum opinion filed on the 28th day of November, 1924, counsel for plaintiff submitted a draft of his proposed findings and defendant's counsel offered the objection that the fixing of the date of the transfer of West's stock to Sears as the first day of December, 1920, was not justified by the evidence, particularly as it was claimed by counsel that the stubs in the stock certificate book, to which had been attached the reissued certificates as transferred from West to Sears indicated that those certificates were written up by the secretary on November 17, 1920; and that such fact, being considered in connection with the testimony of Norsworthy, determined the correctness of the defendant's conten-

tion. I have since made a painstaking examination of the stock book, the certificates as last issued to Sears, and the testimony to which my attention has been attracted.

The fact to be determined is as to when the transaction by which West relieved himself of his ownership interest in the stock of the cotton company was completed. The best conclusion that I am able to arrive at, considering all of the circumstances, and considering the admitted fact that the promissory note which Sears agreed to furnish to West evidencing his indebtedness for the purchase price of the stock was not delivered until some time in December, 1920, is that the date of December 1st, 1920, should be allowed to stand. Norsworthy did testify that he put the proper dates on West's certificates when he first reissued them in Sears' name; and that he erased such dates because Sears and West wanted the certificates dated May 24, 1920. He testified that he could not tell what the date as first inserted, and which was erased by him, had been, and was unable upon an examination of the stock certificate book to tell what date had been erased. Witness Hartke, who was secretary of the cotton company in the latter part of 1920, testified that he saw the figures as originally written by Norsworthy; that Norsworthy had first written in "December first" or "the numerals corresponding to that date". I think that it may be fairly said that a real uncertainty, judging even from the stub certificate record alone, as to what the erased dates were and as to whether such dates did represent the real date of

the transaction, exists. I find that on the stubs representing the reissued certificates the figures representing the year have been changed on several of the stubs. If the May date and the November date claimed, were both of the same year, I cannot understand why, if the figures "20" after the printed "19" had been written in first under the November date, those figures should have been erased and the same figures rewritten in the space. Turning again to the stubs of the stock certificate book, to which the original certificates of West had been attached and across which the word "Cancelled" has been written, evidently at the time of the reissue to Sears, it appears that the cancellation date has been there inserted and evidently erased and no new date substituted. On stub No. 3 there is an indication that the cancellation date, which was erased, began with the letter "D", which would suggest that December might have been written therein. At any rate, the evidence furnished by the certificate book of itself is not satisfactory enough to warrant a definite determination even that Norsworthy issued the new certificates to Sears and sent them to West on the date claimed in November. But as I have stated even though that fact did appear, it devolves upon the court to determine when the transaction was really closed.

Findings may be prepared making the date as heretofore indicated, to-wit, December 1st, 1920, as being the time when Sears obtained complete ownership of the cotton company.

Dated this 23rd day of February, 1925.

Wm. P. James

District Judge.



[Endorsed]: No. 1124-Civil. U. S. DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA. SOUTHERN DIVISION. THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, Defendant. MEMORANDUM SUPPLEMENTAL OPINION. FILED FEB 23 1925 CHAS. N. WILLIAMS, Clerk By Murrav E. Wire Deputy Clerk

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At a stated term, to wit: the January, A. D., 1925 Term of the District Court of the United States of America, within and for the Southern Division of the Southern District of California, held at the Court Room thereof, in the City of Los Angeles, on Monday, the twenty-third day of February, in the year of our Lord one thousand nine hundred and twenty-five;

Present:

The Honorable Wm. P. James, District Judge.

Citizens National Bank, Plaintiff, )

vs. )

No. 1124 Civ. )

Maryland Casualty Co., Defendant. )

This cause having been further considered by the court re the transfer of Wests's stock to Sears, the court hands down a memorandum supplemental opinion, which is ordered filed herein, and orders findings may be prepared making date as heretofore indicated, to wit: December 1st, 1920 as being the time Sears obtained complete ownership of the Cotton Company.

IN THE *SUPERIOR* COURT OF THE UNITED  
STATES FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES, )	
a corporation, )	No. 1124-Civil
Plaintiff, )	
vs. )	RECEIPT OF
MARYLAND CASUALTY )	PROPOSED BILL
COMPANY, a corporation, )	OF EXCEPTIONS
Defendant. )	

Receipt of copy of Proposed Bill of Exceptions in the above entitled matter received this 8th day of June, 1925. Consisting of 188 pages.

Hunsaker, Britt & Cosgrove

Attorneys for Plaintiff

Receipt of copy of Amended Proposed Bill of Exceptions in the above entitled matter received this 27th day of July 1925. Consisting of 257 pages.

Hunsaker, Britt & Cosgrove

Attorneys for Plaintiff

(Testimony of Thomas W. McDevitt.)

IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES, )	
a corporation, )	
Plaintiff, )	
vs. )	BILL OF EXCEP-
	TIONS
MARYLAND CASUALTY )	
COMPANY, a corporation, )	
Defendant. )	

BE IT REMEMBERED that the above entitled action came on regularly for trial on the 20th day of December, 1923, before Hon. William P. James Judge sitting in above entitled Court, without a jury, trial by jury having been waived; plaintiff being represented by Messrs. Hunsaker, Britt & Cosgrove; and the defendant appearing by Messrs. Bicksler, Smith & Parke, the following proceedings and none other were had and the following evidence and none other was received.

TESTIMONY OF THOMAS W. McDEVITT

Thereupon, Thomas W. McDevitt, a witness for and on behalf of plaintiff, being duly sworn, testified as follows:

I have been a resident of Los Angeles for thirteen years and was President of the Cotton Company. I was acquainted with Mr. J. B. Sears. He died on the 3rd day of May, 1921, he having committed suicide by shooting himself.

(Testimony of Thomas W. McDevitt.)

Whereupon the plaintiff introduced in evidence as plaintiff's Exhibit No. 1, the application of the Cotton Company to the defendant for the bond sued upon and the application of J. B. Sears to the defendant, marked plaintiff's Exhibit No. 2, and the bond issued by the defendant to the Cotton Company, being the bond sued upon in this action, and which bond is marked Plaintiff's Exhibit No. 3, which said Plaintiff's Exhibits, 1, 2 and 3, are as follows:

Plaintiffs Ex #1

Employees, Agents, &c.

FIDELITY SECTION

MARYLAND CASUALTY COMPANY

Home Office: Baltimore, Md.

The applicant will please answer fully all questions asked. Confidence must be reposed in the Company if confidence is expected in return. All information received is used solely by the Company in judging the risk, and will be treated as STRICTLY CONFIDENTIAL.

=====

1 I hereby make application for a bond for \$50,-  
2 000.00 to date from November 1st 1919 and affirm  
that in the following declarations made, I state  
the truth without reservation.

3 Name J. B. Sears of Los Angeles, Cal.  
4 Residence street and number? 1438 So. Hobart  
Bld. Age 37 years.

5 Where were you born? Waco, Texas  
(Nationality American  
(Race White

6 How long have you lived in this Country?



(Testimony of Thomas W. McDevitt.)

7    If a naturalized citizen of the United States, give  
      date of naturalization, where and in what court.

8    Date      x      , in      x      , at      x

---

(Name of Court) (Place and State)

9    Married or Single? Married    How many persons  
      are dependent on you?    One

10   Full name of your wife    Itylene Weakley Sears  
      Her Address      Same

APPLICANT WILL PLEASE STATE  
 NAMES AND ADDRESSES OF PAR-  
 ENTS IF LIVING, OR OTHER NEAR-  
 EST RELATIVE

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	Name	Relation	Occupation	Address
11				
12	Dr. R. C. Brown	Uncle	M. D.	Waco, Texas

---

13   To whom is bond to be given?

     California Cotton & Factorage Co.

     (Give exact title of firm, company or organization)

14   Home office of employer?    Los Angeles, Cal.  
      Business?    Cotton

15   Where will you be employed?    Los Angeles, Cal.  
      Title of Position?    Manager & Secretary

16   State your duties in that position—Buying & Sell-  
      ing cotton.

---

17   How long have you been in the continuous service  
      of Employer requiring this bond?    In what po-  
      sition?    Where located?    Date of taking pres-  
      ent position requiring this bond

(Testimony of Thomas W. McDevitt.)

18 Ans. About 6 mo.      Manager      Los Angeles  
Sept. 1st 1919

---

19 Who will pay the premium for this bond? California Cotton & Factorage Co.

20 Have you previously given bond to the above employer? No. Amount? \$———

21 Who furnished it? X      Why discontinued?

21 Has your application for a bond ever been declined? No. By whom?

23 What salary or compensation will you receive?  
\$5,000.00

24 Are you responsible for any portion of losses that may be occasioned by bad credits given? Give particulars

25 No.

---

## YOUR OCCUPATION THROUGHOUT THE LAST TEN YEARS

Please give, accurately, particulars of your OCCUPATIONS OR EMPLOYMENTS during the PAST TEN YEARS, showing the full disposition of your time, WHETHER YOU WERE EMPLOYED OR NOT. If you were at school or college during any part of the period, give particulars of attendance at each school with name and address of your teachers. Begin in the top space with the most recent period. If the space is insufficient, please complete the record on a separate sheet.

IF UNEMPLOYED FOR A GIVEN TIME—GIVE  
NAMES OF TWO PERSONS WHO CAN  
VERIFY THE FACT.

---

(Testimony of Thomas W. McDevitt.)

FROM	TO	Give name or exact style (if firm or corporation) of your Employer and his business address.	Town & Street Address & place where you worked	Name and present address of party under whom you worked
		<p>Last 18 to 19 years Geo. H. McFadden Bros. Agcy. W. J. Meale, Agent, Waco, Texas</p>	<p>Nature of your position or occupa- tion.</p>	<p>Why did you leave.</p>
			<p>The Bond Will not be Is- sued Unless Complete In- formation is Given in these Spaces.</p>	

- 26 If bonded in any of above positions, state which  
and give name of Company or person acting  
as your surety, also address.
- 27 Answer—Was bonded but do not know name.
- 28 Have you income other than your salary as above  
stated? No. How much?.....yearly.
- 29 From what source?.....  
(State fully whether in such  
employment you are engaged for  
your own account or in the em-  
ploy of another.)
- 30 Are you now and will you continue to be thus  
engaged?
- 31 Do you own any real estate? (Location) Yes  
Corpus Christie, Texas  
Value? \$ Est. \$5000
- 32 Do you own any personal estate? (Character)  
.....Value? \$.....
- 33 Is there any encumbrance on your property?  
(Character) Amount? \$.....
- 34 Are your parents possessed of any property?  
(Character) Value? \$.....
- 35 State amount of your debts and liabilities other  
than liens on property? \$.....
- 36 If other than current bills, explain nature of your  
debts and state what effort you are making to  
liquidate same.
- 37 .....
- 38 .....
- 39 Is your life insured? Yes To what amount?  
6,000.00 State nature of policies and to whom



- 40      payable?    Wife
- 41    Do you ever engage in speculative transactions?
- 42    No.    Of what nature?.....
- 43    Do you use intoxicating liquors as a beverage? No.
- 44    Were you ever in business on your own account?  
       No.    Where? .....
- 45    When?    From                      to
- 46    Reason for discontinuing same?
- 47    Give names and addresses of partners, if any
- 48    Have you ever failed in business or made com-  
       promise with creditors?
- Ans. ....
- 49    If so, state when?..... Where?..... Business
- 50    Name of firm.....Assets \$....Liabilities \$....
- 51    Name and present address of Assignee or Trustee
- 52    Has final settlement been made?.....  
       On what basis?.....
- 53    Names and addresses of (3) largest Creditors...
- 54    .....
- 55    Have you ever been in arrears or default in your  
       present, or any previous employment?.....
- NOTE: If answered "Yes," give particulars in  
       separate confidential letter to the Company.

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## REFERENCES

Give at least five.    Write names and addresses  
plainly.    Do not give former employers as references.

---

Names of References	Occupation	P. O. Address
1. W. J. Meale	Waco, Texas	
2.	Agt.	
3.	Geo. H. McFadden & Bros.	
4.		
5.		

=====

The MARYLAND CASUALTY COMPANY, (Hereinafter called Company) is hereby authorized, without further request from me, to execute, as surety, or to procure the execution of not only the bond herein applied for, but any and all bonds which may be required of me in the service of this, or any other employer, and to consent, as often as it may deem necessary to a change in such bonds or the bond herein applied for, or any of them, so as to cover me in a different position, or amount, or in the service of a different employer.

And in consideration of the execution, or procurement, of such bonds by the Company, I agree to pay the Company an annual premium in advance of . . . . . Dollars, (\$ . . . . .) for the bond herein applied for, and such other premium or premiums as may be agreed upon for any other bond or bonds which the Company may execute or procure; and I do further agree to indemnify the Company against all loss, liability, costs, damages, charges and expenses whatever which the Company may sustain or incur by reason of having executed, or procured the execution of, the bond herein particularly applied for, or any of the bonds which said Company

is, by this instrument, authorized to execute or procure, or any renewal or continuance of any of the aforesaid bonds, including counsel and attorney's fees which it may incur in connection with any litigation or investigation relating to its rights or liabilities under any of said bonds; and I do agree to pay all expenses including reasonable attorney's fees that the Company may incur in enforcing any of the agreements herein contained. And I do further agree that the vouchers or other evidence of payment of any such loss, liability, costs, damages, charges or expenses shall be taken as prima facie evidence against me and my estate of the fact and extent of my liability to the Company.

I hereby further agree that the Company shall have the absolute right to decline to issue any such bond, or if any such bond be issued, to decline to renew or continue same, and to cancel at any time any such bond or any renewal or continuance thereof; and that the Company shall be under no obligation to disclose its reasons therefor or to give any information in connection therewith, the provisions of any law to the contrary being hereby expressly waived by me.

And as an additional consideration, I hereby waive all right to claim any of my property, including my homestead, as exempt from levy, execution, sale or other legal process under the laws of this or of any other state.

IN WITNESS WHEREOF, I hereunto set my hand and seal this 1st day of December, 1919.

Witness J. F. Norsworthy

J. B. Sears (Seal)

Plaintiffs Ex. #2

No.....

FIDELITY SECTION  
BONDING DEPARTMENT  
MARYLAND CASUALTY COMPANY  
BALTIMORE

.....191....

California Cotton & Factorage Co.  
548 Merchants National Bank Bldg.,  
Los Angeles, Calif.

An Application has been made to this Company to issue to you a Fidelity Bond for Mr. J. B. Sears as Secretary & Manager in your service, at Los Angeles, Calif., to the amount of \$50,000.00

Before passing on the said Application the Company must have answers to the following questions:

Very respectfully yours,  
Jno. T. Stone,  
President.

ANSWERS

QUESTIONS

- 1 To whom is the bond to be made payable?
  - (a). Give exact title.
  - (b). State Employer's line of business.
- 2 From what date is it to be written and for what amount?
  - a California Cotton & Factorage Co.
  - b Buying and selling cotton.

From Nov. 1st, 1919, for \$50,000.00



- 3 (a). What is the title of the applicant's position?  
 (b). If traveling salesman, who will pay his traveling expenses?  
 (c). At what place will he be employed?  
 (d). Explain fully his duties.
- 4 Who will pay the premium on the bond?
- 5 (a). From when does his present employment date?  
 (b). Has the applicant previously been in your employ?  
 (c). Has the applicant been under bond to you?  
 (d). Why is change now desired?  
 (e). Have you any knowledge or any information or are you aware of any habit of the applicant or any circumstances which might unfavorably affect the risk to the surety on the bond applied for? If so, state particulars.
- a Secretary & Manager  
 b .....  
 c Los Angeles, Cal.  
 d Will run the business.  
 California Cotton & Factorage Co.  
 a Sept. 1st, 1919  
 b From....No..., 19..., to....., 19....  
 c.....No..... Surety.....  
 d .....  
 e None .....

- 6 (a). If paid by salary, state amount and when payable.  
(b). If applicant will be remunerated by you on any other basis, state nature of the engagement, with amount of applicant's monthly earnings. (Attach copy of Contract, if any.)  
(c). If a salesman, will applicant be charged with any portion of losses arising from bad credits?  
(d). If a salesman, will he be required to remit all collections immediately to Home Office?
  7. (a). If applicant's duties embrace the custody of CASH, state LARGEST amount likely to be under his or her control at any one time.  
(b). For what length of time is applicant apt to have control of such amount?
- a \$5,000.00 per year payable monthly as a minimum guarantee on
  - b 25% of the profits. Contract not yet drawn up.
  - c .....
  - d .....
  - a Cash be in bank
  - b No cash in personal control, only as checks may be issued or received for deposit.

(c). Will applicant have control of securities?

(d). If so, state value of same, whether negotiable, and if such securities are under joint control with some other officer.

8 (a). Will applicant be authorized to pay out of the CASH in his or her custody any amount on your account?

(b). In what manner is such authority given?

9 (a). If applicant's duties embrace custody of goods or samples, give particulars, stating probable maximum value.

(b). How often, in what manner, and by whom will inventory of such stock of goods and samples be taken?

NOTE:—It is necessary that this Form be fully completed. (OVER)

BOND CANNOT BE EXECUTED UNTIL THIS FORM IS FULLY COMPLETED AND RETURNED TO THE COMPANY.

c .....

d Negotiable all of them and under his control.

a All things paid by check

b By-laws.

a .....

b .....

NOTE: It is necessary that this form be fully completed  
ANSWERS

# QUESTIONS

- 10 (a). How often and to whom will applicant remit or pay over money received?
- (b). Will applicant be permitted to retain any balance on hand; if so, about how much, and for what purpose?
- (c). If required to deposit in Banks, state in what name accounts will be kept.
- (d). Will applicant or the Bank be required to send you duplicate deposit slips or receipts?
- (e). State whether applicant can ENDORSE checks drawn to your order, and for what purpose.
- 11 (a). Will applicant be authorized to sign checks on your behalf?
- (b). Will the COUNTERSIGNATURE of any person be invariably required; if so, whose?

a Money be deposited as received.

b No cash except in bank.

c California Cotton and Factorage.

d .....

e Yes for deposit.

a Yes he is manager.

b No the owners live in other cities.



- 12 (a). At what intervals will applicant's books, accounts, stock and securities be inspected and audited and verified with funds on hand or in bank?
- (b). At what intervals and in what manner will outstanding accounts, as shown by applicant's books or reports, be verified?
- (c). If salesman or collector, how often do you bill the trade direct?
- (d). By whom will above inspections and audits be made?
- 13 (a). Has applicant always faithfully, honestly and punctually accounted to you for all moneys and property heretofore under his control or custody as your employee?
- a Yes
- a. Books checked at least once in every .....month. Books checked up each month.
- b. We have no such accounts.
- c. ....
- d T. J. West Treasurer.....official capacity.

(b). Are applicant's accounts at this date in every respect correct, and proper securities, property and funds on hand to balance his accounts?

b Yes.  
a No.

14 (a). Is applicant now in debt to you?  
(b). If so, state amount and nature of such indebtedness, and if secured, how?

b .....

15 Have you ever sustained loss through the dishonesty of any one holding the position of the applicant, or holding a similar position?

No.

16 (a). Will you require additional surety from the applicant other than the amount applied for to this Company?

a No.

(b). If so, state amount, and by whom given?

b .....

It is agreed that the above answers are warranties and constitute the basis of and form a part of the consideration of the bond executed or about to be executed by the MARYLAND CASUALTY COMPANY in favor of the undersigned upon the person above named, and also all continuations or renewals thereof or substitutions therefor, until superseded by other written answers similarly furnished to and accepted by the said Company.

Dated at Calexico, Calif., this 28th day of November, 1919.

Signature of employer—CALIFORNIA COTTON &  
FACTORAGE CO.

By T. J. West

Treasurer Official Capacity.

If the employer (the obligee in the bond) be an individual, he must sign this statement; if a firm, one of the firm must sign the firm name and his own; if a corporation, it must be signed by an executive officer and returned to the Home Office of the Company at Baltimore, Md.

Plaintiffs Ex 3.

“Register No. 5493. (\$2.50 cancelled revenue  
stamps attached)

MARYLAND CASUALTY COMPANY  
BALTIMORE

---

WHEREAS, J. B. Sears, hereinafter called the Employee, has been appointed to a position in the service of California Cotton & Factorage Co., Los Angeles, Cal. hereinafter called the Employer, and

WHEREAS, said Employee has been required to furnish Bond.

NOW, THEREFORE, in consideration of a certain premium to be paid annually in advance during the term of this bond, and of the Employer's written statements relative to the Employee, his duties and accounts, it is hereby agreed that the MARYLAND CASUALTY COMPANY, a corporation of Maryland, hereinafter called the Company, will, within two (2) months after the receipt of satisfactory proofs of loss, reimburse the Employer for any loss, not exceeding Fifty Thousand Dollars (\$50,000), of money, securities or other personal property (including that for which the Employer may be responsible to others), which the Employer shall have sustained by reason of any act or acts of FRAUD, DISHONESTY, FORGERY, EMBEZZLEMENT, WRONGFUL ABSTRACTION or WILFUL MISAPPLICATION on the part of the Employee, while in the performance of his duties as Secretary in the service of said Employer and, occurring during the continuance of this bond.



THIS BOND is executed upon the following express conditions; which are conditions precedent to the right of the Employer to recover hereunder;

1. That the term of this bond begins at noon on the 1st day of November A. D., 1919, and ends with (a) the permanent or temporary retirement of the Employee from the service of the Employer; (b) the discovery by the Employer of loss hereunder; or (c) the cancellation of this Bond by the Employer or the Company.

2. That all statements which the Employer has furnished to the Company concerning the Employee or his duties or accounts are warranted by the Employer to be true; that the Employer has no knowledge of any act of fraud or dishonesty committed by the Employee while in the service of the Employer or elsewhere; that if the Employer become aware of the Employee committing any act of fraud or dishonesty, or of the Employee gambling or speculating or committing any disreputable, lewd or unlawful act, the Employer shall, within ten (10) days thereafter, notify the Company by registered letter, addressed to the Company at its Home Office, Baltimore, Maryland, and the Company shall not be liable for any loss subsequently incurred by the Employer through any act of the Employee unless the Company shall have consented, in writing, to continue its liability under this bond.

3. That any loss covered hereunder be discovered during the continuance of this bond or within six (6) months after its termination, and notice of such loss

be sent by telegraph and by registered letter, both addressed to the Company at its Home Office, Baltimore, Maryland, within ten (10) days after the discovery; that an itemized statement of the loss shall be filed with the Company by the Employer within ninety (90) days after the date of said notice of loss; that if required by the Company, the Employer shall produce for investigation all books, vouchers, and evidence in the Employer's possession, and render every assistance (except pecuniary) capable of being rendered by the Employer, that may aid in bringing the Employee to justice.

4. That the Employer and the Company shall share any recovery (excluding insurance and reinsurance), made by either on account of any loss, in the proportion that the amount of the loss borne by each bears to the total amount of the loss.

5. That this bond may be terminated by the Company upon fifteen (15) days' notice, in writing, to the Employer and likewise the Employer may terminate this bond by notice in writing to the Company, specifying the date of cancellation. Upon the termination of the bond and provided no loss has been reported, the Company shall refund pro rata, unearned premium.

6. That should the Employee become guilty of any criminal offence covered *covered* by this bond, the Employer shall immediately, on being requested by the Company so to do, lay proper information before an officer or other body having authority to issue warrant for the arrest of the Employee, and verify the same as required by law, and furnish the Company every

aid and assistance (not pecuniary) that can be rendered by the Employer his agents or servants, in the apprehension and prosecution of the Employee.

7. That should the Employer and the Company disagree regarding the amount of any claim made under this bond, the amount may, at the election of the Employer or the Company be determined by arbitrators; one to be selected by the Employer, one to be selected by the Company, and a third (in the event of failure to agree upon the amount of the claim) by the two so selected; the written decision of the majority of said arbitrators shall be binding and conclusive as to the amount of such claim and the total expense of such arbitration shall be paid by the Company.

8. That no action or proceeding shall be brought to recover any claim under this bond unless begun within twelve (12) months from the time detailed statement of loss shall have been given to the Company by the Employer, unless by statute of the state in which suit is brought agreements such as in this condition contained are expressly prohibited.

SIGNED, sealed and dated this 19th day of December, A. D. 1919.

Not valid unless countersigned by an authorized official or agent of the Company.

E. E. Holly

---

Assistant Secretary.  
(SEAL)

Jno. T. Stone  
President.

Countersigned at Philadelphia, Pennsylvania this  
26th day of December, A. D. 1919.

Louis J. Farley

---

attorney-in-fact."

Indorsed as follows:— "No. 134580  
ENTERED LINE SHEET 5080 REGISTER R-410  
MARYLAND CASUALTY COMPANY  
INDIVIDUAL BOND  
\$50,000  
ON BEHALF OF  
J. B. Sears  
to  
California Cotton & Factorage Co.  
Los Angeles, Cal.  
Dated November 1st, 1919.  
For Transfers or Renewal,  
Apply to  
HASELTINE SMITH,  
FIRE, LIFE AND GENERAL INSURANCE,  
326 Walnut St. Phila."

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That plaintiff thereupon offered and there was received in evidence as Plaintiff's Exhibit 4, the By-Laws of the California Cotton and Factorage Company and Sections 1 and 4 of Article 3 and Article 4 thereof were read into evidence as follows:

"Article 3: Officers: Section 1, Executive Officers. The executive officers of this corporation shall be a president, vice-president, secretary, who shall also be



the general manager of the corporation, and a treasurer, all of whom shall be elected by the board of directors; any one of whom is qualified to hold any one of the above named offices." Section 4 reads—"Section 4: Secretary and General Manager. The secretary shall keep full minutes of all of the stockholders' meetings of the board of directors, in the books provided for that purpose; he shall attend to the giving and serving of all notices for the corporation; he shall keep the seal of the corporation and shall affix said seal to all certificates of stock, contracts and other instruments in writing executed in the name of the corporation; he shall have charge of the book of blank certificates of stock; shall fill out and sign as secretary all the certificates of stock issued, and shall make corresponding entries upon the margin of such books and papers as the president may direct. He shall keep a proper stock and transfer book, showing the names of the stockholders, the number of the shares issued to each stockholders, and the date of such issuance; he shall attend to the correspondence in the name of the corporation and perform such other duties as shall from time to time be assigned to him by the president and as are required of him by law and the By-Laws of the corporation." "The secretary of this corporation shall also be the general manager and any and all contracts made, agreements entered into or instruments signed, checks or drafts issued, notes or any obligations signed or created by him as such general manager, shall be valid and binding upon the corporation without the previous authorization or subse-

quent ratification of the president or any other officer or member of the corporation, and said general manager is hereby given complete and unrestricted power and authority to enter into any contracts or agreements and perform any and all acts and things necessary and in line with the carrying out and fulfilling of the purposes of this corporation and connected with his duties as the general manager thereof, in the performance of which duties his authority is absolute and unrestricted."

#### Article IV.

##### Certificates of Stock and Transfers.

##### Section 1. Certificates of Stock.

Certificates of stock shall be of such form and device as the board of directors shall direct and shall each be signed by the president and countersigned by the secretary, and express on the face the number and person to whom it is issued. The certificate book shall contain a margin on which shall be written the number, date and number of shares and the name of the person holding same as expressed in the corresponding certificate.

##### Section 2. Transfer of Stock.

Shares of the corporation may be transferred at any time by the holders thereof, or by the attorney legally constituted or by any legal representative, by endorsement on the certificate of stock. But no transfer shall be valid until the surrender of the certificate and the acknowledgment of the transfer on the books of the corporation.

##### Section 3. Old Certificates to be cancelled.

(Testimony of L. C. Ivey.)

No surrendered certificates shall be cancelled by the secretary before a new one is issued in lieu thereof, and the secretary shall preserve the certificate so cancelled as a voucher however if a certificate is lost or destroyed, and the board shall order a new certificate issued upon such guarantees by the parties claiming same, as they deem necessary.

#### TESTIMONY OF L. O. IVEY

L. C. Ivey, a witness for plaintiff, being first duly sworn, testified as follows:

I reside in Los Angeles and am at present a vice-president of the Citizens National Bank. During November 1919 and May 1920 I was assistant cashier, and during the year of 1919, and until the first of June, 1921, I was in charge of the note department of said bank, and in fact still have charge of that department.

Whereupon, the plaintiff offered in evidence as plaintiff's exhibit 5, the following letter, written on letter head of California Cotton and Factorage Company:—

“Los Angeles, Cal. Sept. 8th, 1919.

Mr. A. J. Waters, Pres. Citizens National Bank, Los Angeles, Cal. Dear Sir: Complying with your request today, the following is a general outline of the business to be conducted by the California Cotton and Factorage Co.

The Company is incorporated for \$100,000.00 Capital Stock, of which \$50,000.00 is paid in.

Officers of the Corporation are:

(Testimony of L. C. Ivey.)

T. W. McDevitt—Pres. Also Pres. California Cotton Oil Co.

J. P. Conduit—V. Pres. also V. Pres. California Cotton Oil Co.

T. J. West—Treas. also Pres. T. J. West Co. Calexico.

J. B. Sears—Secy. Mgr.

The majority of the stock is controlled by T. J. West of the T. J. West Co., Calexico, who is Treasurer.

The purpose of the Corporation is the buying, selling and the handling of cotton in bale form in all its different branches, or in other words to do a general legitimate cotton business, which will at all times be on a regular basis and as far from speculation as possible.

The financing of the cotton bought or sold will at all times be protected by collateral either in the form of Warehouse Receipts or Railroad Bills of Lading, which will be held by the Bank as security together with actual daily balances. These Warehouse Receipts or Bills of Lading will at times have to be replaced with Trust Receipts, in order to facilitate the movement of the cotton, for example in making shipments from the different interior points, it is necessary to have the Warehouse Receipts in order to secure the cotton and get Bills of Lading for shipments and at such times Trust Receipts will be issued by ourselves until we can secure the Outbound Bills of Lading, after which time Bills of Lading attached to Sight Drafts are returned to the Bank and the Trust Receipts taken up.



(Testimony of L. C. Ivey.)

All purchases or sales will at all times be protected, either by Actual Sales or Purchases or Hedged in the New York or New Orleans Future market.

The manner of payment for actual cotton bought will be in the form of Acceptances protected by Warehouse Receipts or Bills of Lading covering the actual number of bales of cotton bought or sold, which will also be covered by Insurance in the form of a Blanket Policy for the amount of \$100,000.00.

It is the purpose of the Company at all times to carry sufficient daily balance to protect its trades, as well as security with collateral attached.

The total amount of the Acceptance account will vary according to the promptness in making shipments and we do not at any time expect to carry a stock of more than three to five hundred bales and this stock will be covered by actual sales or hedges..

The Acceptance Account will in some instances run as high as \$150,000.00 to \$200,000.00, but as an average this will probably be between \$50,000.00 to \$75,000.00, which will be protected by either Warehouse Receipts or Bills of Lading.

The consignment end of the business will of course depend on the amount of this kind of business that you care to take care of and on the disposition of the planter, as to holding for higher prices, but the advances on this character of business will not exceed from one half to three quarters of the value of the cotton protected by Warehouse Receipts and endorsed notes, which will be held by yourselves.

(Testimony of L. C. Ivey.)

The rate of Interest on the Acceptance Account, as paid in the past by both McFadden Agency and Fowler & Co., was from six to seven per cent and on Eastern drafts interest was charged until the drafts were reported paid. In some instances during the last two seasons  $\frac{1}{8}$  of 1% exchange was charged on Eastern Drafts instead of the interest charge and credit was given for the face of the draft at time of deposit.

It is very hard to cover in detail the business as a whole, but we have given you in a general way that which we think is of interest.

We enclose herewith letter from Messrs. Geo. H. McFadden & Bro's. Agency, Waco, Texas, for your information and trust that we have covered about what you wish.

Yours very truly,  
California Cotton and Factorage Co.,  
BY J. B. Sears."

It was stipulated by counsel that this letter marked 'Plaintiff's exhibit 5' was received by Mr. Waters of the Citizens National Bank on or about the 8th day of September, 1919.

I was acquainted with J. B. Sears and did business with him at the bank. I was familiar with the letter, plaintiff's exhibit 5, and was familiar with the manner in which the business outlined therein was transacted. Mr. Sears had general conversations with me respecting the manner in which the company transacted its business, but he did not ever tell me that the business of the Cotton Company with the Bank was being handled in any other way. I had conversations with Mr.

(Testimony of L. C. Ivey.)

Sears at the banking room of the Citizens National Bank regarding the business between the Bank and the Cotton Company at or about the time the account was first opened, about 1919, and as late as May 1921. No third person was present when I had these conversations with Mr. Sears except at the time he was called in; he had a conversation with Mr. Waters a few days before he died.

“Q I want to know now what Mr. Sears said to you respecting the manner in which they were doing business; in other words, tell the court what Sears said to you between those intervals you have just mentioned in the bank respecting their manner of doing business.

A I cannot remember any specific instance regarding the specific manner. It was understood it was to be carried out in accordance with the terms of that letter.

Q Did he ever tell you that it would be necessary to take out the cotton tickets and give trust receipts?

A Yes, that was understood.”

I cannot, however, recall that Sears ever told me that fact.

Whereupon, eighty-seven sight drafts bearing numbers consecutively from 77 to 162 were exhibited to the witness, who identified them as being in his charge in the note department of the plaintiff bank. It was stipulated that the endorsement or stamp of the Superior Court of Los Angeles County upon said drafts was placed there in a certain action brought on said drafts in said Superior Court and was not there at the time the bank held them.



(Testimony of L. C. Ivey.)

The witness being shown one of said drafts and asked to explain the manner in which the said drafts came into the hands of the plaintiff bank, testified as follows:

They were sent to the bank in most cases by some outside correspondent bank and were received through the mails. The draft of November 8, 1920, in the sum of \$2675.25 bears the number "36" and was drawn by the Calxico National Bank upon the California Cotton and Factorage Company and was sent to plaintiff bank through the mail. The stamp "Accepted, California Cotton and Factorage Company, J. B. Sears, Manager; the Citizens National Bank, Los Angeles, California," was not upon said draft or any of the 87 drafts at the time they were received by plaintiff bank. The acceptance thereon became affixed in the following manner. The acceptance stamp was placed on the drafts by the bank awaiting the signature of Mr. Sears on behalf of the Cotton Company and the acceptance would then be signed by Mr. Sears either at the bank or in case he was busy, it would be sent by messenger to the office of the Cotton Company. The signature of J. B. Sears appearing under the acceptance stamp on each of the 87 acceptances is the genuine signature of J. B. Sears. The notation upon said draft of "A/C of" followed by the figures "25 c-r" means 25 cotton receipts. At the time this draft No. 36 was received by the plaintiff bank there was attached to it 25 cotton receipts or yard tickets. There were yard tickets attached to each of the 87 drafts in varying amounts and the sight draft indi-



(Testimony of L. C. Ivey.)

cated the number of yard tickets which were attached by a similar notation to that explained above. After the drafts had been accepted by the Cotton Company through J. B. Sears, Manager, the plaintiff bank would deliver to Mr. Sears, on behalf of the Cotton Company, the yard tickets attached to the draft and take a trust receipt in lieu thereof.

Whereupon, the 87 sight drafts were introduced in evidence as plaintiff's exhibit 6, said sight drafts with the acceptances thereon being all substantially as follows, save and except as to date and amount and number of yard tickets attached, to-wit:—

Plf. Ex. "6"

Cotton Draft

California Cotton & Factorage Co. No. 736

(Blue Ink Stamp:)

COTTON

21937

Los Angeles, California

Calexico Cali 11/18 1920

At sight

PAY TO THE ORDER OF

Calexico Natl Bank . . . . \$2,675/25 Two Thousand Six  
Hundred Seventy Five and 25/100 Dollars VALUE  
RECEIVED AND CHARGE TO ACCOUNT OF

of

A/C/25 C/R B/C—MARKED B/L No.

or

W. H. Rept. . . . .

(Testimony of L. C. Ivey.)

(Stamped in red ink)

108798

ATTACHED....TOTAL WT.

To California Cotton & Factorage Co.

Through Citizens Natl Bank

Los Angeles Cali

Calexico National Bank

E. W. Beidleman A. C.

(Stamped in blue ink:)

Date NOV 19 1920

ACCEPTED

CALIFORNIA COTTON & FACTORAGE CO.

By J. B. Sears

Manager

*Thu* CITIZENS NATIONAL BANK

Los Angeles, Calif.

TELLER No. 1

(Stamped across face in red ink:)

Judgment entered hereon in the

Superior Court of Los Angeles

County, State of California,

this 9 day of May, 1922

L. E. LAMPTON, County Clerk

By F. E. Langford, Deputy.

(Indorsed on back:)

Without recourse

Calexico National Bank

E. W. Beidleman A. C.

(Testimony of L. C. Ivey.)

(Stamped):

PAY TO THE ORDER OF  
ANY BANK, BANKER OR  
TRUST CO. ALL PRIOR  
ENDORSEMENTS GUARANTEED

90-518

CALEXICO NATIONAL BANK  
CALEXICO, CALIFORNIA

(Indorsed:) T. W. McDevitt

I hereby guarantee payment of the  
within note, or bill of exchange, or  
any renewal or extension thereof (in-  
cluding reasonable attorney fees),  
incurred in enforcing this guaranty,  
and waive demand, presentment for pay-  
ment, protest and notice of protest,  
and consent that the time for payment  
be extended without notice to me.

(Signed) T. W. McDevitt

“MR. PARKE: I have no objection to the introduction except we do desire to call the court’s attention to the fact that they are accepted as “manager”, and, insofar as they attempt to bind the surety company for any liability on account of his acts limited as secretary, we offer the objection that these drafts are immaterial.

THE COURT: That is a matter, of course, which you will want to argue at the conclusion of the case.

MR. PARKE: Yes.

(Testimony of L. C. Ivey.)

THE COURT: Objection over-ruled.

MR. COSGROVE: It may be stipulated the total is \$82,487.96?

MR. PARKE: If you will so state.

MR. COSGROVE: Yes, as pleaded in the complaint.

MR. PARKE: May we have an exception to your Honor's ruling?

THE COURT: Yes."

It was stipulated that the total of the 87 drafts, plaintiff's exhibit 6, aggregates \$82,487.96.

Whereupon, there was exhibited to the witness 87 trust receipts numbered consecutively from 77 to 162, which were identified as the trust receipts introduced in the previous trial of this action, and it was stipulated that the signature of J. B. Sears thereon was his genuine signature. The trust receipts were identified by the witness as those delivered to the plaintiff bank in lieu of yard tickets or cotton receipts surrendered to the Cotton Company and which cotton tickets were originally attached to the sight drafts. Said 87 trust receipts were thereupon introduced in evidence as plaintiff's exhibit 7 and were, save and except as to date and amount in words and figures as follows, to-wit:

"California Cotton & TRUST RECEIPT No.....  
Factorage Co.  
Cotton.

Los Angeles, California,.....

Received in trust from The Citizens National Bank  
of Los Angeles.....Bank of Los Angeles.....



(Testimony of L. C. Ivey.)

documents, described below, the purpose being to secure delivery of the shipments and secure outbound documents therefor, which shall be returned to said bank in cancellation of this receipt.

B/L No.....No. B/C.....Mark.....

CALIFORNIA COTTON & FACTORAGE CO.

Compress or yard receipts                      J. B. Sears                      Mgr."

.....B/C attached

Q Now, what is the \$2,293.60; what is the significance of that, if you know?

A That was the amount of the draft to which the 21 bales of cotton, as indicated in the receipt, was attached.

Q That was the amount of the sight draft which had been accepted at the time that this trust receipt was given?

A Yes.

Q And this figure "21 B/C", what does that mean?

A Bales of cotton."

Whereupon counsel for plaintiff read into the record from the minutes of meetings of the Board of Directors of plaintiff bank certain extracts referring to the manner of extension of credit by the Bank to the Cotton Company. The following was read from the minutes held September 11, 1919.

"Upon motion of G. W. Walker, seconded by A. J. Waters and carried, a line of credit up to the maximum amount of \$200,000.00 at any one time was granted to the California Cotton and Factorage Company, the same to be guaranteed by its officers and

(Testimony of L. C. Ivey.)

secured by warehouse receipts for cotton, drafts with bills of lading attached for cotton or advances to growers on crop mortgage of cotton. Signed M. J. Monette, Chairman pro tem, attest, E. W. Pettigrew, Secretary."

Mr. G. W. Walker was a director of the plaintiff bank and Mr. A. J. Waters was president and also a director.

The following excerpts were read from the minutes of a meeting of the Board of Directors held June 22, 1920.

"Upon motion of George W. Walker, seconded by M. J. Monette, and carried, the California Cotton and Factorage Company was granted a line of credit up to \$75,000.00 to be secured by notes of cotton growers, which in turn are to be secured by chattel mortgage on growing cotton crops, the notes of the Company to draw interest at ten per cent per annum, such line of credit granted with the understanding that \$25,000.00 of the loan be carried in the form of a certificate of deposit. Signed M. J. Connell, Chairman, J. M. Rugg, assistant secretary."

The total number of cotton tickets attached to the 87 drafts and for which trust receipts were issued and delivered to the bank in lieu thereof aggregate 1,476 and represent that number of bales of cotton. After Mr. Sears' death, 385 of the cotton tickets were returned to the plaintiff bank and disposed of by it.

Q "Now, did you ever discover, or were you *were* informed that Mr. Sears or the California Cotton and

(Testimony of L. C. Ivey.)

Factorage Company was disposing or had disposed of cotton tickets for which you held trust receipts?

MR. PARKE: We object to that, if your Honor please, as incompetent, irrelevant, immaterial, whether this particular witness knew, it appearing from the allegations of the complaint that tickets, for which trust receipts were issued, were turned over by the bank pursuant to an arrangement by which the California Cotton and Factorage Company should sell and dispose thereof, and they allege further in the complaint that they were sold and disposed of, and the outbound documents covering the same were deposited in the Citizens National Bank and it would be immaterial whether this particular officer of the bank knew all of the facts in connection with the transaction, it affirmatively appearing that the bank did know from some of the other officers of that fact.

MR COSGROVE: We don't accept those statements that any of the officers knew it. What we are trying to show is that the officers of the bank did not know it. Now, I am producing the officer who has charge of the acceptance account and we expect to produce the three vice presidents and prove that they didn't know anything about it, either, and we expect to show by this witness that the first time that he learned that there was a violation of the terms of the trust receipt was after this man had shot himself and I expect to show then what, if any action, he took in connection with it.

MR. PARKE: Mr. Cosgrove, you don't mean to say or state or contend that you will produce testimony



(Testimony of L. C. Ivey.)

to show that the bank did not know that the acceptances which were paid were being paid out of cotton sales?

MR. COSGROVE: That hasn't anything to do with the question I am asking this witness. The question is whether or not he knew that Sears was disposing of that cotton in violation of the terms of his trust receipt.

MR. PARKE: Well, if that is the purpose of it I object to it on the ground that it calls for a conclusion of the witness. If he will ask whether or not this witness knew whether Sears was disposing of the cotton covered by the trust receipt I think that far he may go.

MR. COSGROVE: That is not the question I asked. If I had asked the witness the question which I put here a minute ago it would be objectionable on that ground. I would like to have the question read.

THE COURT: All right.

(Question read.)

THE COURT: He may answer the question.

MR. PARKE: Note an exception.

A. Not until May 19, 1921, when Mr. McDevitt came into the bank and said that."

I remember the occasion of Mr. Sears' death. I had a conference immediately prior thereto in the office of the plaintiff bank. Mr. A. J. Waters was president. Mr. Sears came to the bank at the request of Mr. Waters. I telephoned to Mr. Sears and told him that Mr. Waters would like to talk to him concerning the acceptance account of the Cotton Company and for him to come to the bank. The occasion of my notify-



(Testimony of L. C. Ivey.)

ing Mr. Sears to appear at the bank was that the acceptance account had not been moving for some time, that is, the cotton was not coming and going, and I had noticed about that time a drop in cotton, which I called to the attention of Mr. Waters. Mr. Waters said: 'Well, get in touch with Mr. Sears and have him come in.' When I telephoned Mr. Sears he stated he would come in the next morning, which he did. At this conversation Mr. Waters stated to Mr. Sears that the acceptance account was not moving very fast and the price of cotton was going down and that the bank was expecting a visit from the National Bank Examiner and the bank would like to have the cotton tickets returned to the bank in lieu of the trust receipts which it held and that Mr. Sears said "all right—I have them down in my safe and I will bring them or send them up to you right away." Mr. Waters replied: "Very well, that will fix it up." Mr. A. J. Waters is now deceased; his death occurred prior to the first trial of this case. Mr. Sears did not bring up the cotton tickets and I telephoned him again and he made some excuse that he would send them right in, or that he was busy, or something to that effect. The conversation in the presence of Mr. Waters, as above stated, took place on or about the 20th day of April, 1921, and Mr. Sears died on the morning of May 1, 1921. I think I telephoned to Mr. Sears two or three times between the date of that conversation and the date he committed suicide and he never did produce the cotton tickets.

(Testimony of L. C. Ivey.)

On the 19th day of May, Mr. McDevitt, President of the Cotton Company, came in and stated that the books of the Cotton Company were being checked by an auditor and that he had reported a shortage in the cotton tickets covered by trust receipts held by the bank. I thereupon took the matter up with Mr. Cosgrove, attorney for the bank. I endeavored to secure portions of certain sight drafts that the Cotton Company had put through the bank and upon which it had gotten credit for the money evidenced thereby. I was successful in securing a return of two of these sight drafts which had been put through covering cotton sold, and which sight drafts, accompanied by bills of lading for cotton sold, were drawn upon the purchaser of said cotton as drawee. The two sight drafts which the bank recovered were one dated December 16, 1920, and one dated April 29, 1921. It was stipulated that the signature of J. B. Sears, Manager of the California Cotton and Factorage Company, attached to said two sight drafts was his genuine signature. Thereupon, the two sight drafts were exhibited to the witness who further testified as follows: "These two drafts were passed through the Citizens National Bank. The fact that each draft has an O. K. and the initials of one of the vice presidents of the bank on it and also the endorsement stamp of the Citizens National Bank indicates this fact. The earlier draft, that dated December 16, 1920, contains an O. K. and the initials J. M. R. These initials are those of J. M. Rugg who was at that time and still is a vice president of the plaintiff bank. On the draft of April 29, 1921,

(Testimony of L. C. Ivey.)

the initials E. T. P. appear, being those of Mr. Pettigrew, at that time a vice president. I am familiar with Mr. Rugg's O. K. and with the signature, handwriting and initials of Mr. Pettigrew. The bank gave to the Cotton Company credit for the amount of the sight drafts. The O. K. by one of the bank's vice presidents is a notification to the teller that immediate credit for the amount of the sight draft should be given to the Cotton Company and characterizes the transaction as a cash transaction as distinguished from an item for collection." Without the approval of the Vice-President such a draft would have to be deposited for collection, but when approved it is handled as a cash deposit and entitled the depositor to entry upon its deposit books and upon the books of the bank, the same as if so much currency had been deposited.

Whereupon, the said two sight drafts were introduced in evidence and marked plaintiff's exhibit 8.

(Plaintiff's Exhibit No. 8)

COTTON DRAFT

CALIFORNIA COTTON & FACTORAGE CO.

No. 332

COTTON

(Stamped) 39905

Los Angeles, California

APRIL 29 1921

\*\*\*\*\*ON DEMAND\*\*\*\*\*PAY TO THE  
ORDER OF CITIZENS NATIONAL BANK OF  
LOS ANGELES\*\*\*\*\*\$1596.78

(Testimony of L. C. Ivey.)

PAY \$1596 AND 78 CTS.....DOLLARS  
VALUE RECEIVED AND CHARGE TO AC-  
COUNT OF

A/C OF FIFTY B/C-MARKED GRAB B/L No.

OR

W. H. Rept

B/L

INV. ATTACHED 26613#

CONF. TOTAL WT.

To PACIFIC COTTON MILLS CO: INC.)

ALHAMBRA: CALIFORNIA. )

California Cotton & Factorage Co.

By J. B. Sears

Manager

E. T. P.

(STAMPED ACROSS FACE IN RED INK):

P A I D

W

W

7

MAY 3, 1921

7

ALHAMBRA

SAVINGS AND COMMERCIAL BANK

ALHAMBRA, CAL

(Stamped across back in purple ink):

PAY TO THE ORDER OF

ANY BANK OR BANKER

The Citizens National Bank

OF LOS ANGELES, CAL.

Collection Department

H. D. IVEY, Cashier.



(Testimony of L. C. Ivey.)

(Plaintiff's Exhibit No. 8)

(Written in Ink)

130 34

COTTON DRAFT

California Cotton & Factorage Co.    No. 321

(Stamped in

COTTON        green ink) 34630

LOS ANGELES, CALIFORNIA

Dec--16th--1920.

.....DEMAND-----PAY TO THE ORDER OF  
Our-Selves-----\$11535.85  
Eleven Thousand Five Hundred Thirty Five & 85/100  
-----DOLLARS

Value Received and Charge

To Account Of

A/C OF 142    B/C -MARKED Various

B/L No. 11 ATTACHED    69404

~~OR~~

TOTAL WT.

~~W. H. REPT.~~

To Stewart Bros Cotton Co.

NEW ORLEANS, LA.

California Cotton & Factorage Co.

By J. B. Sears

Manager

J. M. R.

(Stamped across face in blue ink)

NEW ORLEANS BRANCH

FEDERAL RESERVE BANK OF

ATLANTA

NEW ORLEANS, LA.

(Testimony of L. C. Ivey.)

(Indorsed on back)

California Cotton & Factorage Co.

By J. B. Sears

Manager

(Stamped in purple ink:)

PAY TO THE ORDER OF ANY  
FEDERAL RESERVE BANK  
FOR COLLECTION ONLY

16-16 DEC 16 1920 16-16

LOS ANGELES BRANCH  
FEDERAL RESERVE BANK OF  
SAN FRANCISCO

(Stamped in purple ink)

PAY TO THE ORDER OF  
ANY BANK OR BANKER

The Citizens National Bank  
OF LOS ANGELES, CAL.

Collection Department

H. D. Ivey, Cashier

(Stamped in blue ink)

Left by.....

FEDERAL RESERVE BANK

It was thereupon stipulated that all outbound drafts were passed on by the bank to the drawee and that the drawee in turn took them up and the money came back to the Citizens National Bank. That said sight drafts, plaintiff's exhibit 8, were the usual and customary form of sight draft with bill of lading attached.

(Testimony of L. C. Ivey.)

Whereupon, the bank pass book of the Cotton Company was offered and received in evidence as plaintiff's exhibit 9. It was stipulated that said pass book was used by the Cotton Company during the time covered by the transactions in dispute herein; and it was further stipulated that said pass books showed that the sight drafts, plaintiff's exhibit 8, were credited in the pass book on the same date as that of said drafts, and it was stipulated that a like entry was made in the pass book as a deposit in the amount of all other sight drafts so deposited.

Whereupon, plaintiff introduced letters dated September 12, 1919 and August 14, 1922, written and delivered to Mr. Sears, which letters are as follows:

"To Whom it may Concern:—

This letter will serve to introduce Mr. J. B. Sears, Manager of the California Cotton & Factorage Company, of this city.

This company has recently been organized, with a substantial paid up capital, for the purpose of buying and selling cotton in all of its different branches, and the stockholders of the company are gentlemen in good standing and representing considerable responsibility.

Mr. Sears is recommended to us very highly, and we have confidence in his ability to manage the business successfully.

We have agreed to extend credit to the company, secured by cotton, to the extent of \$200,000, which amount, we are informed by the officers, will be sufficient, in addition to the capital paid in to the company, to take care of their requirements this season.

(Testimony of Thomas W. McDevitt.)

Thanking you for any consideration you may show Mr. Sears, we are

Very truly yours,

(Signed) A. J. Waters, President."

"Los Angeles, Cal. August 14th, 1920.

To Whom it may Concern: This will be presented by Mr. J. B. Sears, General Manager of the California Cotton Factorage Company, with headquarters in Los Angeles and Calexico.

This company has done a very large business with us for the last number of years, and has always maintained liberal balances and carried out it's contracts with us in a very satisfactory manner.

Mr. Sears has acted as general manager, and we have a great deal of confidence in his ability and integrity.

We do not feel that Mr. Sears, or the California Cotton & Factorage Company, would enter into any contract that they were not prepared to faithfully carry out.

Yours truly,

(Signed) W. J. Doran, Vice President."

Said letters were received in evidence as plaintiff's exhibit No. 10.

#### FURTHER TESTIMONY OF

THOMAS W. McDEVITT

THOMAS W. McDEVITT,

witness for plaintiff, was recalled:

#### DIRECT EXAMINATION

During the two years preceding May 1, 1921, I had offices adjoining those of the Cotton Company and



(Testimony of Thomas W. McDevitt.)

saw Mr. Sears frequently. I took no part in the practical operation of the affairs of the Cotton Company. As president, I presided at the directors' meetings and was able to influence considerable business in favor of the Company, but I wasn't a practical technical cotton man and wasn't active in the practical technical end of it. I did not buy or sell any cotton. I discussed with Mr. Sears the affairs of the Cotton Company frequently and saw about a dozen statements that Mr. Sears had prepared reflecting the financial condition of the Cotton Company. Monthly statements were prepared under the supervision of Mr. Sears, and were retained in his possession. Shortly after the first of the month, Mr. Sears would show me a statement and Mr. Sears did say that he would forward a copy of such statement to Mr. West at Calxico. Whether he did forward such copies, I do not know. The last statement of the Company I saw was two or three months prior to Sears' death. During the year preceding Sears' death, I had frequent talks with him concerning the financial affairs of the Cotton Company—probably as many as half a dozen. In substance, Mr. Sears would explain that the Company had bought so much cotton at various places—that the market was going down, but that the Cotton Company was protected by "hedges".

"THE WITNESS: A "hedge" of cotton is selling it the day you buy it, selling it on the board the day you buy it, or selling it on the board the day you buy to protect against a loss."

(Testimony of Thomas W. McDevitt.)

Mr. Sears would just talk to me in general terms about how much cotton the Company had bought and that there was a good outlet for it at a good price. And he handed me a statement of the business showing that so much cotton had been bought and sold and that the expenses of the Company were so much. He informed me that we made money. I do not have any of the statements which he gave me. I do not know what became of them. The last I saw of them was previous to Mr. Sears' death. The statements were uniform as to the manner of setting up the business—they would show on one side the assets of the Company and on the other side the liabilities; the amount of cash in bank; the amount of cotton on hand; the cost of doing business; and the profit during the period the statement covered. On the 29th of April, 1921, Mr. Sears advised me that the Company was losing money. This was about five o'clock in the afternoon of April 30th, at the office of the Cotton Company in the Merchants National Bank Building. I had talked to him on the 29th day of April, 1921, about 9:30 a. m. I called him on the telephone and told him that the Citizens National Bank acceptance accounts seemed to be unduly large and asked him if the Cotton Company had cotton tickets to cover it, to which Sears replied "yes". I then asked him to get up a statement for the bank and he said he would have it a little later. About three o'clock p. m., I called him and he said he would have the statement by five o'clock p. m.

(Testimony of Thomas W. McDevitt.)

“Q Did he come into your office?

A I pushed the buzzer and he came into my office. He said “We have lost some money.” I said, “how much?” He said, “I don’t know.” “Well,” I said, “let’s find out.” He says, “We have some cotton tickets in the bank for which we haven’t the cotton.

Q Did he say, “cotton tickets in the bank” or “Trust Receipts?”

A Cotton tickets.

Q What, if anything, did you say to that?

A I said, “Does the bank know it?” And he said, “No.”

Sears then told me he had trust receipts in the bank for cotton and that the Company did not have the cotton. I asked him if he knew that it was a penitentiary offense. I asked him to prepare a statement and meet me at the bank at nine a. m. the next morning to check up with the bank and find out where the Company stood. I called Sears about nine on the evening of April 29th at his home. I asked him if he had completed his statement and he said “yes”. I told him not to worry; that I would see him in the morning and that the loss was only money and that we would meet at the bank in the morning and fix up whatever loss there was. He thanked me for calling him and hung up the telephone. That is the last conversation I had with him. The following morning I was advised that he had shot himself. I immediately went to Sears’ apartment. Sears was lying unconscious. I arranged for his removal to a hospital and waited



(Testimony of Thomas W. McDevitt.)

until they took him there. I came down town, reaching the Citizens National Bank a few minues before ten. I saw Mr. Waters and told him that Sears had shot himself, and that I did not know the condition of the Cotton Company and suggested that the books be turned over to an accountant to ascertain the true condition, and it was agreed that the books be turned over to R. W. Cole, and there I engaged Mr. Cole to audit the books of the Cotton Company to determine its financial condition. I then returned to the office of the Cotton Company with Mr. Cole's assistant, Mr. Bailey, to whom I turned over the books and accounts of the Cotton Company. On May 19, 1921, Mr. Cole furnished me a verbal report of the condition as disclosed by the audit, which report was in substance that there was a shortage of several hundred bales of cotton in the account of the Company; that there had been deposited in the plaintiff bank trust receipts for which the cotton tickets did not exist. I then informed the bank of that fact, talking to Mr. A. J. Waters and to Mr. J. M. Rugg. Thereupon, accompanied by Mr. Rugg, I went to the office of Hunsaker, Britt & Cosgrove, attorneys for the plaintiff bank, and a telegram was prepared and sent to the defendant notifying them of the loss. Whereupon, the said telegram of May 19th, was introduced in evidence as plaintiff's "Exhibit 11" and read into evidence as follows:

Los Angeles, Calif. 1921. May 19-P. M. 10-03

"Maryland Casualty Company, Baltimore, Maryland.  
The undersigned has sustained a loss of \$50,000.00



(Testimony of Thomas W. McDevitt.)

under the terms of policy Maryland Casualty Company Register No. 5493, growing out of wrongful acts of J. B. Sears, employee, mentioned in said bond. Notice by registered letter follows. California Cotton and Factorage Company, Los Angeles, California."

Whereupon, it was stipulated that the letter of May 19th was written on said date to and received by the defendant on May 25, 1921, which letter is marked "Plaintiff's exhibit 12", and that the letter dated July 22, 1921, together with the proof of loss attached thereto, was written on July 22, 1921, and was received by the defendant on July 27, 1921, said letter being marked "Plaintiff's Exhibit 13" and which said letters, Plaintiff's Exhibits 12 and 13, together with the reply letter of the defendant to the Cotton Company, dated August 9, 1921, (being a portion of plaintiff's Exhibit 13, are as follows:

(Plaintiff's Exhibit No. 12)

CALIFORNIA COTTON & FACTORAGE CO.

J. B. Sears, Secy.-Mgr.

COTTON AND LINTERS

Merchants National Bank Bldg.

LOS ANGELES, CAL.

CODES: SHEPPERSON. 1878-1915

MYERS. 39th Ed.

CABLE: CALIFACT

PHONES: 65171; 61097

POSTOFFICE BOX 443, STATION C.

Agencies:

Calexico, California

(Testimony of Thomas W. McDevitt.)

Blythe, California

Fresno, California

Yuma, Arizona

Phoenix, Arizona

(Stamped in red ink):

SURETY CLAIM DEPART-  
MENT      MAY 25      1921

May

Nineteenth

Nineteen Twenty-One.

Maryland Casualty Company.

Baltimore, Md.

Gentlemen:

In Re: Individual Bond, Register  
No. 5493, California Cotton  
& Factorage Company, Los  
Angeles, Calif., Insured,  
J. B. Sears, Employee.

---

Pursuant to the requirement of Paragrah 3 of the Bond as hereinabove entitled, we are filing herewith and hereby serving notice of loss thereunder. An itemized statement of such loss shall be filed with the Maryland Casualty Company within ninety (90) days from the date hereof.

By reason of acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction and willful misapplication on the part of said J. B. Sears, employee, while in the performance of his duties as Secretary

(Testimony of Thomas W. McDevitt.)

in the service of said California Cotton & Factorage Company, of Los Angeles, Calif., employer, said employer has sustained a loss and shall be responsible to others in an amount of not less than \$50,000.00.

Very respectfully Yours

CALIFORNIA COTTON & FACTORAGE  
COMPANY.

By T. W. McDevitt

President.

(Copy of Letter contained in Plaintiff's Exhibit  
No. 13)

HUNSAKER, BRITT & COSGROVE  
ATTORNEYS AND COUNSELORS AT LAW  
1131-1143 Title Insurance Bldg.  
Fifth and Spring Streets  
LOS ANGELES, CAL.

(Stamped in red ink)

SURETY CLAIM  
DEPARTMENT  
JUL 27 1921

July 22, 1921

In re Bond Register No. 5493—

California Cotton & Factorage Company, Employer;  
J. B. Sears, Employee.

Maryland Casualty Company,  
Baltimore, Maryland.

Gentlemen:

Enclosed herewith we are handing you verified itemized statement of loss as required by paragraph 3 of

(Testimony of Thomas W. McDevitt.)

said bond. Kindly acknowledge receipt of same.

Thanking you for past courtesies, we are

Very truly yours,

CALIFORNIA COTTON & FACTORAGE  
COMPANY,

By T. W. McDevitt

Enc.

President.

PROOF OF LOSS  
MARYLAND CASUALTY COMPANY,  
BALTIMORE, MARYLAND.

Now comes the California Cotton & Factorage Company, a corporation organized and existing under and by virtue of the laws of the State of California, and presents this its ITEMIZED STATEMENT OF LOSS which it has sustained by reason of and resulting from the fraud, dishonesty, forgery, embezzlement, wrongful abstraction willful misapplication and default under BOND NO. 5493, dated the 19th day of December, 1919, said bond being in the amount of \$50,000.00, on behalf of J. B. Sears, employed in the position of secretary to said California Cotton & Factorage Company, a corporation.

DETAILED STATEMENT OF CLAIM:  
PERSONAL ACCOUNT J. B. SEARS:

This account shows in detail all debits and credits passed to Mr. Sears' account. There is an overdraft of five thousand five hundred and three and 88/100 Dollars (\$5,503.88). All original paid bank checks and copies of journal vouchers supporting the debits to this account are now in our possession and subject to your examination.



DEBITS				
Journal Voucher				
Check #1	Sept. 11, 1919,	J. B. Sears	\$1,000.00	
Check #2	Sept. 12, 1919,	J. B. Sears	500.00	
Check #5	Sept. 12, 1919,	Bishop & Bahler Co.	130.70	
Check #35	Sept. 27, 1919,	Bishop & Bahler Co.	.90	
Check #72	Oct. 16, 1919,	J. B. Sears	50.00	
Check #77	Nov. 6, 1919,	J. B. Sears	75.00	
Check #79	Nov. 7, 1919,	Menga & Morev	163.85	
Check #91	Nov. 8, 1919,	J. B. Sears	50.00	
Check #113	Nov. 12, 1919,	Geo. Finks	50.00	
Check #120	Nov. 21, 1919,	J. B. Sears	150.00	
Check #168	Nov. 25, 1919,	J. B. Sears	25.00	
Check #173	Dec. 6, 1919,	J. B. Sears	50.00	
Check #177	Dec. 9, 1919,	Cash	25.00	
Check #182	Dec. 11, 1919,	J. B. Sears	25.00	
	Dec. 13, 1919,	L. W. Stockwell Co. \$29.90		
		Portion chargeable to J. B. S.	14.50	
Check #184	Dec. 15, 1919,	J. B. Sears	30.00	
Check #188	Dec. 18, 1919,	J. B. Sears	25.00	
Check #191	Dec. 20, 1919,	Cash	30.00	
Check #207	Dec. 24, 1919,	J. B. Sears	50.00	
Check #214	Dec. 27, 1919,	J. B. Sears	25.00	
Check #218	Dec. 29, 1919,	J. B. Sears	15.00	

Petty cash					
Check #228	Dec. 30,	1919,	J. B. Sears	24.29	
Check #231	Dec. 31,	1919,	J. B. Sears	20.00	
Check #232	Dec. 31,	1919,	J. B. Sears	135.38	
Check #237	Jan. 1,	1920,	A. B. Williams	110.00	
Check #236	Jan. 3,	1920,	J. B. Sears	250.00	
Check #255	Jan. 2,	1920,	Cash	20.00	
Check #258	Jan. 7,	1920,	T. W. Ewing	8.00	
Check #267	Jan. 7,	1920,	Los Angeles Athletic Club	16.75	
Check #252	Jan. 9,	1920,	Jas. F. Norsworthy	12.00	
Check #272	Jan. 6,	1920,	T. W. Ewing	12.00	
	Jan. 12,	1920,	R. W. Arnold, \$87.50		
			Portion chargeable to Sears	43.75	
Check #273	Jan. 12,	1920,	T. W. Ewing	12.00	
Check #286	Jan. 21,	1920,	First National Bank	100.00	
Check #287	Jan. 21,	1920,	Citizens National Bank	100.00	
Check #301	Jan. 28,	1920,	C. A. Anderson	28.00	
Check #310	Jan. 30,	1920,	Motor Vehicle Dept.	10.00	
Check #312	Jan. 30,	1920,	C. A. Anderson	14.00	
Check #314	Jan. 31,	1920,	Cash	19.50	
Check #316	Feb. 2,	1920,	J. B. Sears	300.00	
Check #342	Feb. 6,	1920,	Cash \$20.00 Db. JBS—	10.00	
Check #345	Feb. 7,	1920,	J. F. Finks	50.00	
Check #378	Feb. 25,	1920,	J. B. Sears	27.00	

Check # 392	Mar. 1, 1920,	T. A. Anderson	50.00
Check # 398	Mar. 2, 1920,	J. B. Sears	300.00
Check # 408	Mar. 5, 1920,	J. B. Sears	25.00
Check # 411	Mar. 5, 1920,	C. A. Anderson	48.00
Check # 418	Mar. 8, 1920,	C. A. Anderson	40.00

\$ 4,270.62

Sub-total

\$ 4,270.62

Balance forward from sheet 2,			
Check # 422	Mar. 3, 1920,	J. B. Sears	50.00
Check # 427	Mar. 12, 1920,	C. A. Anderson	28.00
Check # 435	Mar. 15, 1920,	C. A. Anderson	30.00
Check # 444	Mar. 20, 1920,	J. B. Sears	25.00
Check # 458	Mar. 25, 1920,	C. A. Anderson	27.00
Check # 461	Mar. 26, 1920,	J. B. Sears	75.00
Check # 469	Apr. 1, 1920,	J. B. Sears	250.00
Check # 471	Apr. 1, 1920	C. A. Anderson	36.00
Check # 482	Apr. 3, 1920	T. W. Ewing	25.00
Check # 490	Apr. 8, 1920,	J. B. Sears	35.00
Check # 501	Apr. 13, 1920,	Citizens National Bank	20.00
Check # 506	Apr. 15, 1920,	C. A. Anderson	22.50
Check # 507	Apr. 15, 1920,	Cash	15.00
Check # 511	Apr. 17, 1920,	Cash	15.00

Check #518	Apr. 22, 1920,	J. B. Sears	200.00
Check #521	Apr. 24, 1920,	Cash	25.00
Check #528	Apr. 27, 1920,	I. B. Sears	50.00
Check #479	Apr. 3, 1920,	A. B. Wilman's Co.	110.00
Check #480	Apr. 3, 1920,	I. Walter Reeves	55.00
Check #515	Apr. 20, 1920,	C. A. Anderson	22.50
Check #546	May 5, 1920,	I. B. Sears	15.00
Check #551	May 8, 1920,	I. B. Sears	50.00
Petty Cash	May 19, 1920,	I. B. Sears	27.37
Check #576	May 27, 1920,	I. F. Norworthy \$20.00 JBS—	10.00
Check #580	May 29, 1920,	I. B. Sears	50.00
Check #586	May 31, 1920,	I. B. Sears	300.00
Check #600	June 5, 1920,	I. B. Sears	25.00
Check #611	June 9, 1920,	E. M. Bear \$66.00 Db. JBS	33.00
Check #617	June 10, 1920,	W. M. Markham	25.00
Check #619	June 12, 1920,	I. B. Sears	25.00
Check #632	June 19, 1920,	I. B. Sears	25.00
Check #634	June 22, 1920,	Ed. W. Hopkins, Tax Collector	25.71
Check #637	June 22, 1920,	T. W. Faving	25.00
Check #638	June 25, 1920,	I. B. Sears	75.00
Check #643	June 29, 1920,	I. B. Sears	200.00
Check #641	June 25, 1920,	H. B. Ogden	55.00
Check #654	July 3, 1920,	I. B. Sears	100.00



Check #661	July 3, 1920,	A. B. Wilmans	110.00
Check #667	July 10, 1920,	Fred Johnson \$50.00 Db. JBS	25.00
Check #669	July 12, 1920,	T. J. West	36.00
Check #671	July 13, 1920,	T. W. Ewing	25.00
Check #672	July 14, 1920,	J. B. Sears	300.00
Check #680	July 17, 1920,	J. B. Sears	15.00
Check #686	July 20, 1920,	J. B. Sears	20.00
Check #694	July 23, 1920,	J. B. Sears	72.00
Check #695	July 24, 1920,	J. B. Sears	30.00
Check #700	July 26, 1920,	J. B. Sears	50.00
Check #701	July 27, 1920,	Donavan & Seamans	59.25
Check #706	July 29, 1920,	J. B. Sears	25.00
Check #709	July 31, 1920,	J. B. Sears	20.00
Check #715	Aug. 2, 1920,	J. B. Sears	30.00
Check #717	Aug. 2, 1920,	Will D. Battle	51.00
Check #718	Aug. 2, 1920,	A. B. Wilmans	110.00
Check #719	Aug. 3, 1920,	J. B. Sears	200.00
Check #720	Aug. 3, 1920,	Will D. Battle	10.00
Sub-total			\$ 7,640.95

Balance forward from sheet 3			\$ 7,640.95
Check #737	Aug. 7, 1920,	J. B. Sears	15.00
Check #739	Aug. 9, 1920,	Peter Gluck	100.00
Check #745	Aug. 11, 1920,	J. B. Sears	50.00
Check #747	Aug. 12, 1920,	B. P. Snell	25.00
Check #750	Aug. 14, 1920,	J. B. Sears	500.00
Check #759	Aug. 19, 1920,	L. A. A. Club	18.75
Check #763	Aug. 20, 1920,	Security National Bank	200.00
Check #780	Sept. 1, 1920,	A. B. Wilmans	110.00
Check #781	Sept. 1, 1920,	Security National Bank	200.00
Check #791	Sept. 4, 1920,	Nelson & Price	50.94
Check #797	Sept. 7, 1920,	Walter Nelson \$5.00 Db. JBS.	2.50
Check #806	Sept. 10, 1920,	L. A. A. Club \$24.70 Db. JBS	3.40
Check #816	Sept. 14, 1920,	J. B. Sears	50.00
Check #812	Sept. 11, 1920,	J. B. Sears	20.00
Check #818	Sept. 16, 1920,	Greer-Robbins Co.	200.00
Check #824	Sept. 17, 1920,	J. B. Sears	25.00
Check #825	Sept. 17, 1920,	J. B. Sears	150.00
Check #837	Sept. 23, 1920,	J. B. Sears	25.00
Check #845	Sept. 27, 1920,	J. B. Sears	20.00
Check #852	Sept. 30, 1920,	J. B. Sears	250.00
Check #869	Oct. 4, 1920,	A. B. Wilmans	110.00

Check #878	Oct.	7, 1920,	J. B. Sears	25.00
Check #888	Oct.	9, 1920,	Los Angeles Athletic Club	23.40
Check #889	Oct.	9, 1920,	J. B. Sears	20.00
Check #893	Oct.	12, 1920,	J. B. Sears	100.00
Check #896	Oct.	14, 1920,	J. B. Sears	20.00
Check #902	Oct.	16, 1920,	Greer-Robbins Co.	175.00
Check #909	Oct.	19, 1920,	J. B. Sears \$17.31 Db. JBS	15.00
Check #913	Oct.	21, 1920,	Mrs. J. B. Sears	100.00
Check #919	Oct.	23, 1920,	J. B. Sears	20.00
Check #924	Oct.	25, 1920,	J. B. Sears \$20.00 Db JBS	15.00
Check #926	Oct.	26, 1920,	J. B. Sears	15.00
Check #927	Oct.	28, 1920,	J. B. Sears	75.00
Check #943	Nov.	3, 1920,	J. B. Sears	250.00
Check #948	Nov.	3, 1920,	W. O. Welch, Tax Collector \$8.05—Db. JBS	5.16
Check #961	Nov.	5, 1920,	A. B. Wilmans	110.00
Check #966	Nov.	6, 1920,	J. B. Sears	25.00
Check #975	Nov.	8, 1920,	L. W. Stockwell Co.	13.72
Check #976	Nov.	8, 1920,	L. A. Athletic Club \$14.91 Db. JBS	6.60
Check #986	Nov.	10, 1920,	J. B. Sears	15.00
Check #991	Nov.	13, 1920,	J. B. Sears	25.00
Check #994	Nov.	13, 1920,	John Shepeck	15.00
Journal Entry	Nov.	15, 1920,	J. B. Sears	50.00

Check #1011	Nov. 18, 1920,	J. B. Sears	50.00
Check #1018	Nov. 20, 1920,	J. B. Sears	100.00
Check #1026	Nov. 22, 1920,	J. B. Sears	25.00
Check #1031	Nov. 24, 1920,	A. B. Wilmans	90.00
Check #1050	Dec. 1, 1920,	J. B. Sears	250.00
Check #1053	Dec. 2, 1920,	J. W. McConnell & Sons	12.00
Check #1061	Dec. 6, 1920,	A. B. Wilmans	125.00
Check #1066	Dec. 6, 1920,	So. Cal. Telephone Co.	9.05
Check #1067	Dec. 6, 1920,	Allen McMaster Co.	30.00
Check #1069	Dec. 6, 1920,	J. B. Sears	25.00
Check #1075	Dec. 7, 1920,	Literary Digest	4.00
Check #1081	Dec. 8, 1920,	Automobile Club of So. Calif.	20.66
Sub-total			\$11,626.13
Balance forward from sheet 4			\$ 11,626.13
Check #1084	Dec. 8, 1920,	J. B. Sears	25.00
Check #1089	Dec. 10, 1920,	J. B. Sears	15.00
Check #1093	Dec. 11, 1920,	J. B. Sears	20.00
Check #1100	Dec. 13, 1920,	Mrs. J. B. Sears	100.00
Check #1104	Dec. 14, 1920,	American Circulation Co.	2.00
Check #1108	Dec. 15, 1920,	J. B. Sears	25.00



Check #1115	Dec. 16, 1920,	Donavan & Seamans	8.40
Check #1116	Dec. 16, 1920,	Automobile Club of So. Calif.	42.30
Check #1123	Dec. 18, 1920,	J. B. Sears	25.00
Check #1124	Dec. 20, 1920,	D. S. Greenwood, Secty BPOE	1.00
Check #1129	Dec. 21, 1920,	J. B. Sears	50.00
Check #1130	Dec. 21, 1920,	John Shepek	45.00
Check #1139	Dec. 24, 1920,	J. B. Sears	100.00
Check #1148	Dec. 30, 1920,	John Shepek	25.00
Check #1153	Dec. 31, 1920,	J. B. Sears	25.00
Check #1155	Jan. 3, 1921,	J. B. Sears	300.00
Check #1159	Jan. 4, 1921,	I. F. Norsworthy	153.39
Check #1167	Jan. 6, 1921,	J. B. Sears	25.00
Check #1179	Jan. 10, 1921,	Western Union Tel. Co. \$150.61	
		Db. JBS	
Check #1182	Jan. 10, 1921,	J. B. Sears	6.36
Check #1186	Jan. 11, 1921,	A. B. Wilmans	25.00
Check #1194	Jan. 15, 1921,	John Shepek	75.00
Check #1212	Jan. 17, 1921,	Whitaker Battelle Co.	20.00
Check #1213	Jan. 17, 1921,	Donovan & Seamans	22.50
Check #1218	Jan. 18, 1921,	Dr. Walter Reeves	34.50
Check #1222	Jan. 19, 1921,	J. B. Sears	45.00
Check #1231	Jan. 22, 1921,	J. B. Sears	25.00
Check #1234	Jan. 27, 1921,	J. B. Sears	20.00
			25.00

Check #1240	Jan. 31, 1921,	J. B. Sears	300.00
Check #1246	Feb. 2, 1921,	J. B. Sears	25.00
Check #1261	Feb. 7, 1921,	A. B. Wilmans	125.00
Check #1283	Feb. 10, 1921,	So. Calif. Telephone Co. \$79.10	
		Db. J. B. S.	7.25
Check #1286	Feb. 11, 1921,	J. B. Sears	20.00
Check #1289	Feb. 12, 1921,	Fred T. Johnson	12.00
Check #1294	Feb. 14, 1921,	J. B. Sears	20.00
Check #1305	Feb. 19, 1921,	J. B. Sears	20.00
Check #1309	Feb. 22, 1921,	J. B. Sears \$50.00 Db. JBS	20.00
Check #1314	Feb. 24, 1921,	Brownswood Bulletin	9.00
Check #1315	Feb. 25, 1921,	J. B. Sears	50.00
Check #1323	Feb. 28, 1921,	J. B. Sears	250.00
Check #1329	Mar. 5, 1921,	J. B. Sears \$25.00 Db JBS	11.33
Check #1332	Mar. 7, 1921,	A. B. Wilmans	110.00
Check #1338	Mar. 9, 1921,	J. B. Sears	15.00
Check #1339	Mar. 9, 1921,	Greer-Robbins Co.	12.15
Check #1343	Mar. 9, 1921,	So. Calif. Tel. Co. \$92.50	
		Db. JBS	6.40
Check #1355	Mar. 11, 1921,	Collector Internal Revenue	19.74
Check #1356	Mar. 12, 1921,	J. B. Sears	15.00
Check #1364	Mar. 16, 1921,	J. B. Sears	20.00
Check #1367	Mar. 18, 1921,	Blackstone Institute	20.00

Check #1370	Mar. 19, 1921,	J. B. Sears	20.00
Check #1377	Mar. 22, 1921,	J. B. Sears	20.00
Check #1379	Mar. 22, 1921,	Mrs. J. B. Sears	25.00
Check #1382	Mar. 23, 1921,	J. B. Sears	25.00
Check #1388	Mar. 24, 1921,	Fred T. Johnson	16.00
Check #1390	Mar. 25, 1921,	J. B. Sears	100.00

\$14,205.45

Sub-total

\$14,205.45

Balance forward from sheet 5

Check #1393	Mar. 26, 1921,	J. B. Sears	20.00
Check #1398	Mar. 30, 1921,	J. B. Sears	25.00
Check #1405	Apr. 1, 1921,	J. B. Sears	200.00
Check #1423	Apr. 6, 1921,	J. B. Sears	15.00
Check #1427	Apr. 7, 1921,	A. B. Wilmans	75.00
Check #1428	Apr. 8, 1921,	So. Calif. Tel. Co. \$62.10	
		Db. J. B. S.	3.95
Check #1440	Apr. 8, 1921,	Carmichael Skidmore Co. \$49.40	
		Db. J. B. S.	14.35
Check #1441	Apr. 8, 1921,	I. B. Sears	100.00
Check #1442	Apr. 8, 1921,	G. Hills	10.00
Check #1443	Apr. 9, 1921,	M. J. Collins	75.00

Check #1444	Apr. 9, 1921,	J. B. Sears	50.00
Journal Entry	Apr. 16, 1921,	J. B. Sears	61.08
Check #1456	Apr. 13, 1921,	Blackstone Institute	10.00
Check #1463	Apr. 20, 1921,	J. B. Sears	100.00
Check #1466	Apr. 20, 1921,	S. M. Walker	25.00
Check #1469	Apr. 22, 1921,	R. C. Rowland	8.00
Check #1472	Apr. 22, 1921,	J. B. Sears	25.00
Check #1473	Apr. 22, 1921,	M. F. Shillings	200.00
Journal Entry	Apr. 28, 1921,	J. B. Sears	25.00
Check #1478	Apr. 27, 1921,	Donavan & Seaman	28.00
Check #1480	Apr. 29, 1921,	D. S. Greenwood, B. P. O. E. Lodge	4.50
Check #1487	May 5, 1921,	Carmichael Skidmore Co.	27.39
Sub-total			\$15,307.72

The above checks and journal entries were found to be correctly charged against J. B. Sears' Acct.

The following check was charged against account headed "J. B. Sears, Spl." but should be charged against the personal account;

Check #1169, Jan. 8, 1921, J. B. Sears

100.00



The following checks were wrongfully charged; they are proper charges against J. B. Sears' Acct.

Check #320	Feb. 2, 1920	Cash	15.00
Check #350	Feb. 13, 1920	C. A. Anderson	37.50
Check #512	Apr. 27, 1920,	C. A. Anderson	28.15

The following checks were charged against J. B. Sears, "Suspense" and then wrongfully charged off as Commissions; the same are proper charges against J. B. Sears, Personal Acct.;

Check #148	Dec. 1, 1919	A. B. Wilmans & Co.	800.00
Check #533	Apr. 30, 1920	J. B. Sears	300.00
Check #541	May 3, 1920	A. B. Wilmans	110.00
Check #545	May 5, 1920	Black Wolf Canyon Oil Co.	200.00
Check #606	June 7, 1920	J. B. Sears	200.00
Check #621	June 14, 1920	J. B. Sears	200.00
		Total Debits .....	\$17,298.37

# CREDITS

Sept. 11, 1919—Preliminary Expenses	Sundry	Salary	Expenses
Sept. 27, 1919—L. A. A. Club Fee	\$783.62		
Sept. 27, 1919—Ink Brush	100.00		
	6.90		
		Travel	

Sept. 27, 1919—Expense 9/13-9/27			397.40
Oct. 4, 1919—Expense to Yuma & Blythe			101.05
Oct. 31, 1919—October Salary	300.00		
(August & Sept. Salary )			
(charged direct to Salaries)			
Nov. 21, 1919—Expense to Yuma		50.00	
Nov. 29, 1919—November Salary	300.00		
Dec. 30, 1919—December Salary	300.00		
Jan. 23, 1920—Office Expense			
Jan. 24, 1920—Trip to New Orleans	16.75		616.00
Feb. 3, 1920—January Salary	300.00		
Feb. 28, 1920—February Salary	300.00		
Mar. 30, 1920—March Salary	300.00		
Apr. 26, 1920,—Travel Expenses		173.50	
Apr. 30, 1920—April Salary	300.00		
May 31, 1920—May Salary	300.00		
June 30, 1920—June Salary	300.00		
June 30, 1920—June Travel Expense		172.50	
July 13, 1920—Travel Expenses		137.00	
July 27, 1920—Cash Deposited			
July 31, 1920—July Salary	300.00		
Aug. 31, 1920—August Salary	300.00		
Sept. 4, 1920—Travel Expenses	35.00		153.60

Sept. 7, 1920—Memphis to Boston				600.00
Sept. 30, 1920—12 months at 116.666				
Salary \$5,000 per yr.				
Sept. 30, 1920—September Salary			1,400.00	
Oct. 29, 1920—Travel Expenses			400.00	
Oct. 30, 1920—October Salary			400.00	47.40
Nov. 5, 1920—Travel Expense				
Nov. 30, 1920—November Salary			400.00	150.00
Dec. 30, 1920—December Salary			400.00	
Jan. 3, 1921—Sundry Credits	157.70			
Feb. 3, 1921—January Salary			400.00	
Feb. 28, 1921—February Salary			400.00	
Mar. 31, 1921—March Salary			400.00	
Apr. 13, 1921—Cash Deposited	18.00			
Apr. 30, 1921—April Salary			400.00	
May 9, 1921—Expense Acct.				44.79
		2,517.97	6,500.00	2,643.24
July 1, 1921—8 months @ \$16.66			133.28	
Salary \$5,000 yr.				
		Total Credits	\$11,794.49	
		Total Debits	17,298.37	
		Overdrawn	\$ 5,503.88	

(Testimony of Thomas W. McDevitt.)

ACCOUNT WITH THE CITIZENS NATIONAL  
BANK OF LOS ANGELES:

This is a schedule of accepted drafts due the Citizens National Bank in the amount of eighty-two thousand four hundred eighty-seven and 96/100 (\$82,487.96) dollars. The payment of these drafts was secured by compress or yard receipts for 1476 bales of cotton, which compress or yard receipts were held by the Citizens National Bank as collateral security. J. B. Sears, in the performance of his duties and in the line of his employment as secretary and manager of the California Cotton & Factorage Company, a corporation, took up these compress or yard receipts from the Citizens National Bank of Los Angeles and deposited or substituted in their stead trust receipts, a copy of which is as follows:

TRUST RECEIPT

No. 62

California Cotton & Factorage Co.

Cotton

Los Angeles, California, Nov 15 1920

Received in trust from the

The Citizens National Bank of Los Angeles Bank of Los Angeles documents, described below, the purpose being to secure delivery of the shipments and secure outbound documents therefor, which shall be returned to said bank in cancellation of this receipt.

B/L No.....No. B/C 6 Mark.....

Compress or yard receipts 6 B/C attached

569.61

California Cotton & Factorage Co.

J. B. Sears Mgr.



(Testimony of Thomas W. McDevitt.)

The "outbound documents" mentioned in the trust receipts were never delivered to the Citizens National Bank of Los Angeles, and an examination of the records and files of the California Cotton & Factorage Company formerly in the custody and under the control of said J. B. Sears discloses that of the compress or yard receipts for fourteen hundred seventy six (1476) bales of cotton taken from the Citizens National Bank of Los Angeles by said J. B. Sears in the manner above indicated, compress or yard receipts for but three hundred eighty-five (385) bales of cotton are to be found, and compress or yard receipts for ten hundred ninety-one (1091) bales of cotton are missing and unaccounted for. The receipts on hand for three hundred eighty-five (385) bales of cotton were held by the Citizens National Bank of Los Angeles as collateral for twenty-one thousand eight hundred fifty-nine and 24/100 dollars (\$21,859.24). The receipts unaccounted for and missing for ten hundred ninety-one (1091) bales of cotton were held by the Citizens National Bank of Los Angeles as collateral for sixty thousand six hundred twenty-eight and 72/100 dollars (\$60,628.72).

CALIFORNIA COTTON & FACTORAGE CO.  
SCHEDULE OF ACCEPTED DRAFTS

DUE

CITIZENS NATIONAL BANK

APRIL 30, 1921

Date of Draft 1920.	Drawer	Accepted 1920	Amount	Payee	Number Of		Trust Receipt Deposited By J. B. Sears
					Bales Cotton.		
Nov. 18	Calexico National Bank	Nov. 19	\$ 2,675.25	Calexico National Bank	25		77
Nov. 16	T. W. Ewing	Nov. 20	366.81	E. G. Carruthers State Bank	4		78
Nov. 17	W. T. Carruth	Nov. 22	2,293.60	R. G. Warren	21		79
Nov. 17	W. T. Carruth	Nov. 22	2,632.20	R. G. Warren	34		80
Nov. 18	W. T. Carruth	Nov. 22	4,197.99	R. G. Warren	52		81
Nov. 20	Orcutt Pawley	Nov. 22	465.65	Yuma National Bank	7		82
Nov. 18	T. W. Ewing	Nov. 22	995.27	E. G. Carruthers State Bank	14		83
Nov. 20	W. T. Carruth	Nov. 23	412.46	R. G. Warren	5		84
Nov. 20	W. T. Carruth	Nov. 23	443.65	R. G. Warren	5		85
Nov. 19	W. T. Carruth	Nov. 23	141.23	R. G. Warren	2		86
Nov. 19	W. T. Carruth	Nov. 22	2,455.25	R. G. Warren	35		87
Nov. 20	W. T. Carruth	Nov. 23	1,502.11	R. G. Warren	25		88
Nov. 20	T. W. Ewing	Nov. 24	522.43	E. G. Carruthers State Bank	7		89

Nov. 24	Orcutt Pawley	Nov. 26	331.44	Yuma National Bank	5	90
Nov. 22	W. T. Carruth	Nov. 26	1,414.13	R. G. Warren	23	91
Nov. 22	W. T. Carruth	Nov. 27	395.16	Hellman Comm'l T & S Bank	7	92
Nov. 23	W. T. Carruth	Nov. 27	3,208.94	Jack McDaniels	50	93
Nov. 23	W. T. Carruth	Nov. 27	284.16	R. G. Warren	5	94
Nov. 26	Orcutt Pawley	Nov. 29	2,270.16	Yuma National Bank	35	95
Nov. 23	T. W. Ewing	Nov. 29	130.70	E. G. Caruthers State Bank	2	96
Nov. 30	W. F. Reeves	Nov. 30	293.00	W. F. Reeves	7	97
Nov. 26	W. T. Carruth	Nov. 30	62.47	Hellman Comm'l T. & S Bank	1	98
Nov. 26	W. T. Carruth	Nov. 30	1,352.57	Jack McDaniels	23	99
Nov. 27	W. T. Carruth	Nov. 30	263.23	R. G. Warren	6	100
Nov. 27	W. T. Carruth	Nov. 30	248.23	R. G. Warren	4	101
Nov. 29	Orcutt Pawley	Dec. 1	922.46	Yuma National Bank	15	102
Nov. 29	W. T. Carruth	Dec. 2	1,445.58	R. G. Warren	27	103
Dec. 1	W. T. Carruth	Dec. 4	855.47	R. G. Warren	17	104
Dec. 2	Orcutt Pawley	Dec. 6	676.70	Yuma National Bank	11	105
Dec. 4	Orcutt Pawley	Dec. 7	367.01	Yuma National Bank	6	106
Dec. 6	Calexico National Bank	Dec. 7	6,913.98	Calexico National Bank	76	107
Dec. 4	W. T. Carruth	Dec. 8	1,006.58	Hellman Comm'l T & S Bank	18	108
Dec. 4	W. T. Carruth	Dec. 8	640.74	R. G. Warren	11	109
Dec. 4	W. T. Carruth	Dec. 8	313.45	R. G. Warren	5	110
Dec. 6	S. M. Walker	Dec. 9	117.27	Burton & Williams	2	111

Dec. 4	T. W. Ewing	Dec. 9	778.18	E. G. Caruthers State Bank	12	112
Dec. 6	W. T. Carruth	Dec. 9	605.13	R. G. Warren	10	113
Dec. 8	Orcutt Pawley	Dec. 10	1,783.31	Yuma National Bank	26	114
Dec. 6	T. W. Ewing	Dec. 10	186.65	E. G. Caruthers State Bank	3	115
Dec. 7	T. W. Ewing	Dec. 11	142.49	E. G. Caruthers State Bank	2	116
Dec. 9	Orcutt Pawley	Dec. 13	887.88	Yuma National Bank	14	117
Dec. 9	T. W. Ewing	Dec. 14	128.69	E. G. Caruthers State Bank	2	118
Dec. 15	Calexico National Bank	Dec. 16	8,664.82	Calexico National Bank	89	119
Dec. 13	W. T. Carruth	Dec. 16	589.05	R. G. Warren	10	120
Dec. 13	W. T. Carruth	Dec. 16	186.58	R. G. Warren	3	121
Dec. 15	Orcutt Pawley	Dec. 16	181.30	Yuma National Bank	3	122
Dec. 14	W. T. Carruth	Dec. 17	1,073.90	R. G. Warren	20	123
	Sub-total		57,825.31		786	

Schedule of Accepted Drafts—2

Date of Draft 1920	Drawer	Accepted 1920	Amount	Payee	Number Of Bales Cotton.	Number Of Trust Receipt Deposited By J. B. Sears.
	Amounts Brought Forward		\$57,825.31		786	



Dec. 20	W. T. Carruth	Dec. 23	217.01	R. G. Warren	4	124
Dec. 20	W. T. Carruth	Dec. 23	1,079.56	R. G. Warren	25	125
Dec. 24	W. T. Carruth	Dec. 28	285.70	Hellman Comm'l T & S Bank	5	126
1921						
Jan. 8	W. T. Carruth	Jan. 11	478.29	R. G. Warren	10	127
Jan. 10	Orcutt Pawley	Jan. 13	296.17	Yuma National Bank	5	128
Jan. 10	W. T. Carruth	Jan. 14	585.09	Hellman Comm'l T & S Bank	10	129
Jan. 15	W. T. Carruth	Jan. 18	817.60	R. G. Warren	15	130
Jan. 18	Mrs. M. Ida			Mrs. M. Ida		
	Reeves	Jan. 18	254.20	Reeves	5	131
Jan. 24	Bert P. Snell	Jan. 25	2,000.00	Wm. Loftus, Treasurer	52	132
Jan. 28	W. T. Carruth		301.81	R. G. Warren	5	133
Jan. 28	W. T. Carruth	Feb. 1	201.05	Hellman Comm'l T & S Bank	4	134
Jan. 31	Orcutt Pawley	Feb. 1	2,570.70	Yuma National Bank	37	135
Feb. 1	W. T. Carruth	Feb. 4	258.27	R. G. Warren	5	136
Jan. 31	Orcutt Pawley	Feb. 4	264.00	Yuma National Bank	13	137
Feb. 1	Orcutt Pawley	Feb. 4	45.48	Yuma National Bank	2	138
Feb. 1	Orcutt Pawley	Feb. 4	931.71	Yuma National Bank	13	139
Jan. 31	Orcutt Pawley	Feb. 4	45.40	Yuma National Bank	1	140
Feb. 2	W. T. Carruth	Feb. 7	400.19	R. G. Warren	10	141
Feb. 2	W. T. Carruth	Feb. 7	527.89	R. G. Warren	10	142
Feb. 5	W. T. Carruth	Feb. 8	43.90	Hellman Comm'l T & S Bank	1	143
Feb. 2	W. T. Carruth	Feb. 8	284.42	Jack McDaniels	5	144

Feb. 4	W. T. Carruth	Feb. 8	254.61	Jack McDaniels	5	145
Feb. 8	W. T. Carruth	Feb. 10	527.12	R. G. Warren	10	146
Feb. 15	W. T. Carruth	Feb. 19	754.65	R. G. Warren	15	147
Feb. 15	W. T. Carruth	Feb. 19	256.06	R. G. Warren	5	148
Feb. 15	W. T. Carruth	Feb. 19	405.77	R. G. Warren	10	149
Feb. 19	W. T. Carruth	Feb. 25	214.85	Hellman Comm'l T & S Bank	5	150
Mar. 4	Orcutt Pawley	Mar. 5	898.16	Yuma National Bank	39	151
Mar. 9	W. T. Carruth	Mar. 14	387.51	R. G. Warren	11	152
Mar. 14	First National Bank	Mar. 15	1,920.00	First Nat'l Bank Calexico	20	153
Mar. 22	W. T. Carruth	Mar. 25	168.28	R. G. Warren	5	154
Mar. 24	W. T. Carruth	Mar. 28	318.16	R. G. Warren	8	155
Mar. 26	Orcutt Pawley	Apr. 2	1,261.20	Yuma National Bank	41	157
Mar. 31	Orcutt Pawley	Apr. 4	2,005.70	Yuma National Bank	92	158
Apr. 8	R. G. Warren	Apr. 12	822.50	R. G. Warren	22	159
Apr. 12	First Nat'l Bank, Calexico	Apr. 13	392.00	First Nat'l Bank Calexico	65	160
Apr. 22	South West Cotton Co.	Apr. 25	1,134.36	South West Cotton Co.	52	161
Apr. 22	South West Cotton Co.	Apr. 25	1,053.28	South West Cotton Co.	48	162
Totals			\$82,487.96		1,476	

The above schedule of Accepted Drafts were unpaid on April 30th, 1921. The compress or yard receipts accompanying these drafts, and originally held by the Citizens National Bank as collateral security, have in each case been replaced by a Trust Receipt similar in form to the sample attached hereto and signed by California Cotton & Factorage Co., by J. B. Sears, Manager.

(Testimony of Thomas W. McDevitt.)

SUMMARY OF LOSS:

(a) Overdraft as per itemized account	\$5,503.88
(b) Account with Citizens National Bank of Los Angeles (com- press and yard receipts)	60,628.72
	<hr/>
Total net loss	\$66,132.60

STATE OF CALIFORNIA    )  
                                  ) SS  
COUNTY OF LOS ANGELES )

On this 22nd day of July, 1921, before me Pearl Cunningham a Notary Public in and for the county of Los Angeles, state of California, personally appeared T. W. McDEVITT, to me known, who being first duly sworn according to law, deposes and says: that he is the president of California Cotton & Factorage Company, a corporation, (EMPLOYER), and that the above statement is true and correct in every respect, and that the moneys set opposite the several names listed therein were collected by the said J. B. Sears (EMPLOYEE) on the dates and in the respective amounts set opposite each.

That the sum of \$5,503.88 shown in said itemized statement of overdraft has not been paid over or satisfied in any way whatever to said employer, but has been misappropriated by said employe to his own use and benefit, with the intent to fraudulently deprive the said employer of the same; and that the proceeds of said compress or yard receipts or any moneys, checks, drafts, warehouse receipts, bills of lading or other out-



(Testimony of Thomas W. McDevitt.)

bound documents therefor have not been returned to said Citizens National Bank of Los Angeles, California, in cancellation of trust receipts deposited with said bank by said J. B. Sears in exchange or substitution for said compress or yard receipts, as provided for in the terms of said trust receipts; neither has said J. B. Sears, employe, or said California Cotton & Factorage Company, a corporation, employer, paid over or satisfied in any way whatever to said Citizens National Bank of Los Angeles any moneys in lieu of said compress or yard receipts, and by reason whereof said California Cotton & Factorage Company, a corporation, employer, has, because of said fraud, dishonesty, forgery, embezzlement, wrongful abstraction or willful misapplication of said J. B. Sears, employe, became responsible to said Citizens National Bank.

Further, that there are no offsets whatever against said claim for salaries, commissions or otherwise, other than as set forth particularly in the above statement, and that the said employer has fully complied with all the conditions of the bond issued by the Maryland Casualty Company of Baltimore, on behalf of the said employe, and that said employer has not accepted any security for or on account of the same.

Further the deponent saith that the said employe had been continuously in the employ of the said employer for the period beginning October 1, 1919, and ending April 29, 1921, the employment having been discontinued by reason of the suicide of said employe.

T W. McDevitt

(Testimony of Thomas W. McDevitt.)

Subscribed and sworn to before me, the undersigned,  
at Los Angeles, California, this 22nd day of July,  
1921.

Pearl Cunningham

Notary Public in and for the County of Los  
Angeles, state of California.

134580—Fidelity

California Cotton & Factorage Company  
J. B. Sears

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August 9th, 1921.

California Cotton & Factorage Co.,  
Merchants National Bank Building,  
Los Angeles, California.

Gentlemen:

We are in receipt of your esteemed favor of July 22nd enclosing purported proof of loss on account of alleged peculations of J. B. Sears.

The proof of loss as submitted is hereby respectfully returned as same does not come within the purview of the bond executed.

In connection with this case, please be advised that the Maryland Casualty Company, without prejudice to the rights of any of the parties concerned, is willing to undertake an investigation of the accounts of Mr. Sears, but it must be distinctly understood that in so doing, none of the terms of the bond are waived.

Should it be agreeable for us to proceed as outlined above, we will investigate at once to determine if Mr.

(Testimony of Thomas W. McDevitt.)

Sears has committed any acts for which we, as surety, may be liable.

Awaiting your early wishes in the premises, we are,

Very truly,

G. F. Cushwa.

GFC:MDF.

General Adjuster.

Thereafter, an examination of the books of the Cotton Company were made by Mr. Farrar on behalf of defendant.

“Q During the months or the year immediately preceding May 1st, 1921, did you know that Mr. Sears had sold any cotton for which the Citizens National Bank held trust receipts and used all or any of that money for purposes other than the payment of the acceptances which accompanied the compress tickets or cotton tickets?

MR. PARKE: We object to that, if your Honor please, as incompetent, irrelevant, immaterial, whether this witness knew it or not, it appearing affirmatively from the pleadings and from the testimony introduced by the plaintiff that Sears was vested with full power and authority to handle the business of the Cotton Company as he saw fit and it appearing further that all moneys so used were used in the Cotton Company's business. It is immaterial whether this witness knew whether it was to be applied, that is, whether the proceeds from the sale of cotton represented by the trust receipts was all being applied on the trust receipts or part of its being applied to other obligations of the Cotton Company.

(Testimony of Thomas W. McDevitt.)

MR. COSGROVE: Now, perhaps we can expedite the matter here considerably. Without calling the court at this time to pass upon the relevancy or the materiality and competency of the testimony, may it be stipulated that if it does later appear to be relevant, that this witness will testify, if he were allowed to, and that the fact is that he didn't know that Mr. Sears was using the money for any purpose other than the payment of the indebtedness.

MR. PARKE: Well, I don't see the necessity of a stipulation as to what he would testify, if our objection be good, that it is immaterial whether he knew. He has already testified that he knew nothing about the detail of the operations of the Company's affairs, merely presiding at stockholders' and directors' meetings and that all of the power was delegated to Mr. Sears.

THE COURT: Your position is that if he did know it it wouldn't make any difference?

MR. PARKE: It would make no difference whether he did or did not know it, the whole point being that the application of the funds realized from the sale of this cotton, being all in the Company's business, it is immaterial whether it was properly or improperly applied, so far as the bank is concerned.

THE COURT: I will over rule the objection.

MR. PARKE: Note an exception.

A I did not.

Q Did you, during that time, know that Mr. Sears had sold cotton for which the Citizens National Bank



(Testimony of Thomas W. McDevitt.)

held trust receipts and had gotten the money or had the money put to the credit of the account of the California Cotton and Factorage Company and checked that money out in paying the cost of operating the business of the California Cotton and Factorage Company?

MR. PARKE: May we have the same objection?

THE COURT: Yes; same ruling.

MR. PARKE: Note an exception, please.

A I didn't know it.

Q BY MR. COSGROVE: Did Mr. Sears, during that time, tell you where the money was coming from that was paying the cost of the operating expenses of the California Cotton and Factorage Company?

A He did not."

Mr. Sears reported from time to time that the Company was making money and substantiated his statement by showing to me the monthly statements of the Company which showed an earning, which statements were made to me during the entire operation of the Company.

"Q If you had known in November 1920 or any time thereafter up to and including May 29, 1921, that the money which Mr. Sears was using to defray the expenses of conducting the business of the California Cotton and Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have consented to his continuing the business of the Company.

(Testimony of Thomas W. McDevitt.)

MR. PARKE: I object to that, if the court please, on the grounds heretofore stated, to-wit, that the objection of this witness, as an officer of the Cotton Company, had he known certain facts, is immaterial, it appearing from both the pleadings and the proof of the plaintiff, that the application of the funds to the particular obligations or expenses of the Cotton Company, was a power delegated exclusively to J. B. Sears and it further appearing that all of the application of these funds was on the obligations of the Cotton Company and that it would be immaterial whether this witness, being an officer of the corporation, would or would not have consented to the payment of the operating expenses out of the sale of any particular cotton.

THE COURT: I suppose it may have some bearing on the question of his own vigilance or negligence or lack of vigilance in looking after the affairs and, his state of mind and whether that influenced him in any investigation. I will over rule the objection.

MR. PARKE: May we have an exception?

THE COURT: Yes.

MR. COSGROVE: There are pleadings surely on that point, your Honor.

THE COURT: Very well.

Q BY MR. COSGROVE: Have you in mind the question?

A The question, "Would I have permitted the operations of the Company had I known it?"

Q Would you have consented to it?

(Testimony of Thomas W. McDevitt.)

A I would not.

Q Did you believe the statements that Mr. Sears made to you as you have disclosed them upon the stand?

MR. PARKE: That is objected to as incompetent, irrelevant, immaterial, for the reasons heretofore stated.

THE COURT: Objection over ruled.

MR. PARKE: Note an exception, please.

A Yes, sir.

#### CROSS EXAMINATION

I was president of the Cotton Company from its inception until it went out of business immediately after Mr. Sears' death. During all this time its office was in the same suite of offices as mine in the Merchants National Bank Building, and I was in constant association with Mr. Sears and other employes of the Cotton Company, including Mr. Norsworthy, a book-keeper, and with Mr. Collins who assisted in classing and shipping cotton. The corporation kept books and records of its transactions, but I was not familiar with the books or as to what books were kept. After Mr. Sears' death I turned over to Mr. Bailey all the books that were in the safe. I was not familiar at any time during the two years the Company was doing business with how much it owed to various banks for cotton. I introduced Mr. Sears to Mr. Waters of the Citizens National Bank, and Mr. Sears made the arrangement as set forth in the letter of September 8, 1919, wherein the method of handling the business between



(Testimony of Thomas W. McDevitt.)

the Cotton Company and the Bank was outlined. I saw the letter at the time it was written and was familiar with the arrangements made therein. I have had no experience in the buying and selling of cotton, but have had experience in the growing of cotton and the handling of cotton seed, and I was not familiar with the manner in which the buying and selling of cotton was usually handled by brokerage concerns. The arrangement made by the Cotton Company with the Citizens National Bank was a new arrangement to me. Mr. Sears came to the Cotton Company with a record of having been with the George H. McFadden Company for eighteen to twenty years, working out of their Waco office. It is one of the largest brokerage companies in operation. I do not know whether the arrangement for handling the business between the plaintiff bank and the Cotton Company as outlined in the letter of September 8, was in keeping with the McFadden system of handling such business or not. I personally took no part in any of the transactions between the Cotton Company and the Citizens National Bank, but left all of that business to Mr. Sears.

“Q Now, after the letter, plaintiff’s exhibit 5, was explained to you, you understood, did you not, that the Citizens National Bank would pay the acceptances as they came in?

A Yes, sir.

Q And you understood, did you not, Mr. McDevitt, that the Cotton Company, through Mr. Sears or someone from the office, would arrange to get the



(Testimony of Thomas W. McDevitt.)

cotton tickets from the bank and substitute trust receipts therefor?

A Yes, sir.

Q You knew that arrangement was made early in the negotiations—early in the transaction?

A Yes, sir.

Q You knew, did you not, during this whole period of time that the Cotton Company was securing from the bank the cotton tickets and issuing trust receipts in lieu thereof?

A Yes, sir.

Q. State, if you know, what the purpose of securing these cotton tickets from the bank and substituting trust receipts was; why was it necessary?

A Just what the trust receipt indicated, for the purpose of securing outbound documents and shipping the cotton, getting it released from the warehouse to the railroad.

Q That is, getting the cotton out of the warehouse where it was stored, the warehouse that had issued the cotton tickets?

A Yes, sir.

Q And selling the cotton and getting a bill of lading to attach to the outbound draft?

A Yes.

Q You knew, did you not, that the Cotton Company was selling its cotton as it bought it?

MR. COSGROVE: As it what?

(Testimony of Thomas W. McDevitt.)

Q BY MR. PARKE: That is, I mean, buying it one day and selling it the next day, selling it as rapidly as it could, on the market?

A Yes, sir.

Q That was its business, was it not, buying and selling on quick terms?

A Yes, sir.

Q You knew that all the cotton that came in each day to the Citizens National Bank, evidenced by these cotton tickets, was being sold and disposed of within a very short time by the Cotton Company, did you not?

A Yes, sir.

Q You knew where the Cotton Company was depositing the proceeds from the sale of this cotton, did you not?

A Yes, sir.

Q Where?

A Citizens National Bank.

Q In its checking account?

A Yes, sir.

Q And that met with your approval?

A Yes, sir.

Q You knew that the Cotton Company was paying its acceptances by checks drawn on this checking account, did you not?

A Yes, sir.

Q And that met with your approval?

A Yes, sir."

I knew the Cotton Company had a considerable monthly overhead for operating purposes, including

(Testimony of Thomas W. McDevitt.)

rental and salaries, all of which met with my approval, and I knew that these overhead expenses were being paid by the Cotton Company by checks drawn on its checking account in the plaintiff bank, and such met with my approval.

“Q Now, in answer to Mr. Cosgrove’s question, that if you had known in November, 1920, or at any time thereafter that the money which Mr. Sears was using to defray the expenses of conducting the business of the Cotton Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have permitted him to continue in business; you did know, did you not, that he was paying operating expenses from moneys realized from the sale of cotton, didn’t you?

A Yes, sir.

Q And you knew that cotton had been originally purchased through the Citizens National Bank, didn’t you?

A Yes, sir.

Q You never checked to find out for your own satisfaction whether there was sufficient money to pay for the cotton, that is, to pay for the acceptances and also pay the operating expenses, did you?

A No, sir.

Q You had very little to do with the Cotton Company in any way during the last year, did you not?

A Yes, sir, very little.

Q You were away a great deal of the time?

A Yes, sir.

(Testimony of Thomas W. McDevitt.)

Q The manner of arrangement for payment of expenses and payment of cotton, you referred that entirely to Mr. Sears?

A Yes, sir."

The question of hedging of cotton did not concern me, but was left entirely to Mr. Sears. I do not know the practice in other concerns. The Cotton Company did not hedge as a general practice. It did, however, hedge in a number of instances during both seasons. The books will reflect the statement that the Cotton Company had several thousand dollars worth of hedges. I talked with Mr. Sears about the advisability of hedging. Mr. Sears did not tell me that he had instructions not to hedge from Mr. Neal of Waco, Texas. Mr. Neal was a former employer of Mr. Sears. Mr. Neal played no part in the conduct of the Cotton Company's business. Mr. Neal was connected with the McFadden Company during the time the Cotton Company was in business, and I knew that Mr. Sears relied largely on information received almost daily from the McFadden Agency as to what to do with the cotton which the Company was handling. I was a Director of the Cotton Company, and was doing what I could to direct a considerable volume of business to the Company, telling Mr. Sears where certain cotton could be bought and advising my friends to sell their cotton to the Cotton Company. I had a lively interest in the success of the Company, but no particularly activity in the operation on the practical side of the business, the entire management being left



(Testimony of Thomas W. McDevitt.)

to Mr. Sears. I had nothing to do with the making of certain loans by the Cotton Company to individuals for the growing of cotton crops. Mr. Sears and Mr. West handled the loan of the Cotton Company to the McDevitt Cotton Company in the sum of approximately Sixty Thousand Dollars (\$60,000.00), of which Thirty Thousand Dollars (\$30,000.00) remained unpaid at the end of the first season of the Cotton Company's business, which sum has never been paid, and the Cotton Company holds the McDevitt Cotton Company's note for that amount, but the McDevitt Company is no longer in business. The note, however, was not charged off by the Cotton Company to profit and loss.

I never examined any of the entries in the books of the Cotton Company and never familiarized myself with the financial condition of the Company, except as reflected in the monthly statements brought to me by Mr. Sears. These statements were prepared by Mr. Norsworthy. The Company kept a minute book, wherein was reported the minutes and transactions of the Company's affairs. I knew that the capital invested in the capital stock of the Cotton Company was \$50,000.00. I knew that in addition to the loan made by the Cotton Company to the McDevitt Cotton Company, \$12,000.00 was loaned by the Cotton Company to Pauly at Calxico. I do not recall any other loans.

The Cotton Company did not rely entirely upon the daily transactions to pay its operating expenses. It relied on a certain amount of cotton that it had at the

(Testimony of Thomas W. McDevitt.)

start of the second season on which there was no obligations in the compress at Calxico. I do not recall how many bales there were. I do not know what available assets the company had for operating expenses during the second fiscal year, except that it did have a certain amount of available cotton which was to be collateral for loans. I am familiar with the rise and fall of the cotton market during the years 1919 and 1920. The market was a rising market up until about August 1, 1920—price going as high as 40 cents per pound. The trend of the cotton market during the second fiscal year of the Cotton Company's business, from August 1, 1920, on to about April, 1921, was downward—the price dropping from approximately 40 cents to as low as 8 or 9 cents. About April of 1921 the market took an upward trend. I frequently discussed in a general way with Mr. Sears the trend of the cotton market. He never did tell me that the Cotton Company was losing money, except the day before he died. I made no investigation of my own to ascertain whether Sears was selling the cotton for as high a price as he paid for it, but I did know that the market was gradually going down, and that it did go from 40 cents per pound to 8 cents per pound. I never made any detailed or careful analyses of the monthly statements that were prepared by Mr. Norsworthy. I knew the Company made money the first year.

“Q And its mode or manner of doing business with the Citizens National Bank was the same the first year as the second year?

(Testimony of Thomas W. McDevitt.)

A It was up until the time he performed these irregular acts.

Q BY MR. PARKE: Well, what was the irregularity now that you complain of?

A The irregularity?

Q Yes; I want you to tell the court what was the irregularity in the business transactions between the Cotton Company and the bank, of which you complain.

A Putting a trust receipt in the bank and taking the cotton tickets out for the purpose of shipping them, making no record in the office that we owed the bank for those tickets that were in his possession, and representing to Mr. West and myself that that was our profit, when it really belonged to the bank.

Q You did not consider it an irregularity to give a trust receipt to the bank and take the cotton tickets, did you?

A No, sir.

Q You did not consider it an irregularity for Mr. Sears on behalf of the Cotton Company to sell the cotton covered by those trust receipts, did you?

A No, sir.

Q You did not consider it an irregularity for him, Sears, to take the money realized on this cotton and deposit it in the checking account, did you?

A No, sir.

Q Up to that stage everything was regular?

A Yes, sir.

Q He did that the first year, didn't he?

A Yes, sir.

Q And he did it the second year?

(Testimony of Thomas W. McDevitt.)

A Up until November.

Q Well, he did it during November, didn't he? He got the cotton tickets and sold the cotton and put the money in the bank?

A Yes, sir.

Q He did that just the same during the period when you say there were irregularities as before, did he not?

A Up to that point.

Q Well, up to that point everything was done the same during the period of the irregularities as was done the year before; that is correct?

A No, sir.

Q Well, now, just state again—

A During the year before he applied the proceeds—

Q I am not speaking about that. I am speaking up to the time the money got back in the bank; you were complaining of no irregularities in Mr. Sears taking the cotton tickets from the bank?

A No, sir.

Q And substituting trust receipts?

A No.

Q Do you complain that there was an irregularity in Mr. Sears selling the cotton?

A No, sir.

Q Do you complain that there was any irregularity in Mr. Sears depositing the proceeds from the sale of the cotton evidenced by outbound documents in the checking account?



(Testimony of Thomas W. McDevitt.)

A No, sir.

MR. COSGROVE: I object to that, I would like to have the answer stricken out in order to introduce an objection.

THE COURT: Yes, it will be stricken out.

MR. COSGROVE: We object to that on the ground that it calls for a conclusion on the part of the witness and that it assumes that to which there is no testimony, and that it does not state the facts. Now, I would like to have the question, so that we may not have any misunderstanding of its exact purport.

(Question read)

MR. COSGROVE: The objection to that question, —you see that question does not state the fact. The fact is that Mr. Sears did not deposit any of the proceeds. The fact is that Mr. Sears took these bills of lading with his own sight draft and put them into the bank and got credit upon his books for it, his bank pass book. Sears never deposited the proceeds in the bank.

MR. PARKE: Well, I said proceeds.

MR. COSGROVE: Well, that is all right; if everybody understands it we cannot go astray on it. But, that question is confusing I think, to any one who hears it, the idea that Sears deposited the proceeds from the sale of the cotton. Now, he did not do that. What Sears did was to take the bills of lading and his own sight draft, took that down and got it approved by an officer of the bank and put it in and got credit on his account for it.

(Testimony of Thomas W. McDevitt.)

MR. PARKE: Does counsel mean that if I sell my house today and receive a check drawn on New Orleans and I take the check over and get Mr. Sartori to O. K. it and I deposit it in my checking account, that I cannot be said to have deposited that in my checking account? In that sense I mean that he did deposit the proceeds from the sale. It was not converted into cash for a few days.

THE COURT: You understand between you as to what was done; ask the witness if he had any objection to that.

QUESTION BY MR. PARKE: You had no objections to Mr. Sears depositing the outbound documents representing the sale of cotton in the checking account, did you?

MR. COSGROVE: We object to that question because that is not a fair statement of facts. The fact is, as we all understand it—

MR. PARKE: I am certain that the outbound documents were deposited.

BY THE COURT: Mr. McDevitt, you understand what counsel is referring to, do you not?

A Yes, sir.

Q As to having been done?

A Yes, sir.

Now he asked you whether you had any complaint to make of that.

Q BY MR. PARKE: That is directing his particular attention to the depositing of these outbound drafts with bills of lading attached.

(Testimony of Thomas W. McDevitt.)

MR. COSGROVE: And putting them through as a cash account and getting credit on his account for it, having them enter it as a cash deposit in the cash book.

BY MR. PARKE: Q. You had no objections to that, did you? A. No, sir.

Q What your objection, is it not, Mr. McDevitt, is that he did not pay the acceptances out of the moneys for which he received credit in his pass book; isn't that true?

A What I did object to is that he obtained the cotton tickets for which he gave trust receipts for a specific purpose. He carried the procedure through regularly until he received the credit in the cash book.

Q And then he misapplied the money?

A He did not.

Q You don't claim he misappropriated any money?

A I said he misapplied it.

I consider that he did not during the first year of the Cotton Company's operations apply any portion of the moneys received from the sale of trust cotton in the payment of operating expenses. During the first year the Cotton Company had \$50,000.00 cash to start business with, which money belonged to the Company. I think that that company kept no separate chchecking account, and that the money realized from the sale of trust cotton was deposited together with the money which belonged to the Cotton Company, but I do not know.

"Q How could you tell during the first year when you drew a check against the checking account in which you had deposited the proceeds from the sale

(Testimony of Thomas W. McDevitt.)

of trust cotton that the money was from your funds and not from moneys realized from the sale of that cotton?

A How could we tell it?

Q Yes.

A In the first year there were no demands made on us to pay money which was represented we owed. In the second year when the investigation was made as to the condition of the Company we found out he had dissipated the capital stock.

Q How did he dissipate it; please explain that statement to the court.

A The accountant's statement will show that better than I can explain it.

Q I want you to state. You say you found he had dissipated it. I want you—

A He went to the bank and gave the bank a trust receipt and took out from the bank cotton tickets. He sold that cotton for less than he paid for it. He misapplied the money without notifying the directors that he was operating at a loss and that he did owe the bank money and that he didn't have the money to pay.

Q Is that all the manner in which he dissipated the assets?

A He dissipated the assets in overdrawing his account.

Q To the extent of the checks set up in the bank's second cause of action?

A Yes.

Q He kept full records of everything that was drawn out, did he not?



(Testimony of Thomas W. McDevitt.)

A No, sir, he didn't keep a record of the trust receipts that he owed the bank.

Q I didn't ask you that question.

MR. COSGROVE: We object to argument now.

Q BY MR. PARKE: I asked you if he kept a record of all the moneys he drew out?

A Yes, sir.

Q Did you consider that it was irregular for Mr. Sears to sell the cotton which was bought on acceptances held by the Citizens National Bank for less than he paid for the cotton?

A No, sir.

Q The ability to acquire more or as much as was paid depended upon the market, did it not?

A Yes, sir.

Q How could Mr. Sears have paid the Citizens National Bank in full of its acceptances and discharge the trust receipts, where he was selling the cotton for less than he paid for it?

A He could have acquainted the directors with the fact that he was dissipating the assets, and we would have closed the business.

Q I didn't ask you that. I asked you how he could have paid the bank during this second year?

A He could have paid the bank up to the point that the Company's assets had been used and then he should have notified the Board of Directors that he was working on the bank's money.

Q He did pay the bank up to the full extent of moneys received after payment of overhead operating expenses, didn't he?

(Testimony of Thomas W. McDevitt.)

A I don't know."

I am not familiar with the manner in which checks of the Cotton Company were drawn from the checking account to pay acceptances held by the plaintiff bank. Mr. Conduit, a director, took no active part at all in the handling of the Cotton Company's affairs. Mr. Hartke was secretary and attorney and kept the minute books and attended to the legal affairs of the Cotton Company, but took no active part in the handling of the Company's affairs and had no investment in the Company, acting only as a so-called dummy director. He was secretary for only a portion of the time, as disclosed by the Company's records. Mr. West took a very active part in the handling of the affairs of the Company during the whole period of the Company's operations.

After Mr. Sears' death and at the time I arranged for an examination of the Cotton Company's books by Mr. Cole, I told Mr. Bailey that Mr. Norsworthy and Mr. Collins would give him any help he might require. I ordered the books and records of the Cotton Company removed from its office to Mr. Cole's office, and the safe and everything was moved. The safe and records of the Company, except those produced here in court, are now in Mr. Martin's office in the Cotton Exchange Building, Los Angeles, in the custody of Mr. Martin, and since the time of Mr. Sears' death all the books and records of the Company have been in the custody of Mr. Cole or Mr. Martin.

On the day prior to Mr. Sears' death, when I talked to him regarding the shortage of cotton tickets, he

(Testimony of Thomas W. McDevitt.)

said, "I put trust receipts in the bank for cotton and we have not the cotton." I never discussed with Mr. Sears his personal relationship with Mr. Neal, who was in Los Angeles shortly before Mr. Sears' death. I first ascertained that the Cotton Company owed the plaintiff bank a substantial sum of money on account of acceptances the day prior to Mr. Sears' death. I endorsed all of the acceptances which remained unpaid at the Citizens National Bank at the time of Mr. Sears' death, the endorsement being placed thereon after he died. In the fall of 1920 I talked to Mr. Sears about the financial condition of the Cotton Company and the trend of the cotton market, and he advised me that there was a rather steady decline in the market and expressed the hope that in the near future there would be a break and a trend upwards. *H* never at any time told me that the Company was losing money by reason of the falling market, although he did discuss with me certain individual losses, but I was given to understand in the operations as a whole the Company was making money. I never checked with Mr. Norsworthy at any time the overhead expenses of the Company, and I never checked at any time the cotton tickets on hand in the office of the Cotton Company, or *check* any of the cotton to ascertain its grade and value. In addition to the monthly statements which were prepared, Mr. Norsworthy at the end of the first fiscal year prepared a statement covering the Cotton Company's operations during the preceding year. I do not know where the statement is, but I believe it showed the Company had



(Testimony of Thomas W. McDevitt.)

made money during the first year. I have examined the auditors' report prepared by Mr. Bailey covering the Cotton Company's operations during the second year. and it shows an operating loss.

Practically all of the cotton handled by the Cotton Company was handled through the plaintiff bank.

With regard to the second cause of action will say that there are checks evidencing all of the moneys which it is claimed were overdrawn by Mr. Sears, and all the moneys which Mr. Sears withdrew from the Company's account was evidenced by checks drawn in the regular manner so far as signature and payment by the bank was concerned.

"Q. So far as you know, all of the cotton purchased by the Cotton Company has been accounted for either in the sales that were made or in the tickets that were still on hand?

A Yes, sir.

MR. COSGROVE: That is the allegation of the complaint."

Mr. West did not at any time in my presence discuss with Mr. Sears the affairs of the Cotton Company, although I did hear Mr. Sears outline to Mr. West shortly after the Cotton Company began to do business, the manner in which the Cotton Company was handling its finances with the plaintiff bank, that is, the substitution of trust receipts for the yard tickets, and the substance of such conversation is substantially as set forth in the letter of September 8, 1919, written by Mr. Sears to Mr. Waters. Mr. West agreed that



(Testimony of Thomas W. McDevitt.)

the manner of hand'ing the business between the Cotton Company and the Bank, as outlined in the letter of September 8, 1919, was proper. My statement that Mr. Sears failed to keep in the books of the Cotton Company a record of certain financial transactions is not based upon any examination of the books by myself, but is based upon what others say the books failed to disclose. I do not know whether all the books which were kept by Mr. Norsworthy were actually turned over to Mr. Bailey the auditor. Between the time I introduced Mr. Sears to Mr. Waters and up to the time of Mr. Sears' death I was in and out of the banking house of the plaintiff frequently and discussed the business of the company in a general way with the officials of the bank, but nothing specific. The general nature of the discussions was that the Cotton Company was doing a satisfactory volume of business, that Sears was evidently a practical efficient cotton man and that we were building a nice volume of cotton business.

#### REDIRECT EXAMINATION

Mr. Hartke and Mr. Conduit each had one share of stock in the Cotton Company, and I had one share of stock. Mr. West gave me the one share of stock, and he secured for himself \$49,600.00 worth of stock.

When I said that practically all the cotton came through the Citizens National Bank I meant by that that it was handled through this manner of acceptance. There was, however, cotton purchased through other banks and cotton purchased directly. The

(Testimony of R. W. E. Cole.)

amount of such purchases would be shown in the books; for instance, we might buy from Calexico and ship it within a day or two, and set it out at Calexico, and that amount would not reflect in the Citizens National Bank.

I have a recollection of Sears telling me that he had his cotton hedged during the second year so that the decline would not hurt him.

#### RECROSS EXAMINATION

“Q In that connection you allege in your complaint as one of the bases of your action here, or rather, the Cotton Company does—the bank does, that what Sears did was to go out and speculate upon the market; do you mean by that that he did not hedge?”

A Yes, sir.

MR. COSGROVE: If the court please,—

Q. BY MR. PARKE: I just wanted to know if you called that speculating. If you don't hedge you call that speculation?

A The wildest kind of speculating.”

Testimony of

R. W. E. COLE,

a witness on behalf of plaintiff, being first duly sworn testified as follows:

#### DIRECT EXAMINATION

I reside at San Gabriel, and am a certified public accountant, with my place of business in Los Angeles, having been engaged in that line of work for twenty years. I knew J. B. Sears and E. W. McDevitt, and

(Testimony of R. W. E. Cole.)

have done considerable work for Mr. McDevitt and the companies with which he has been affiliated. On the morning Mr. Sears died Mr. McDevitt came to my office and interviewed myself and Mr. J. S. Bailey and engaged me to prepare a general audit of the books of the California Cotton and Factorage Company. I entrusted this work to Mr. Bailey, who was my supervising accountant, and he accompanied Mr. McDevitt. Later the books of the Cotton Company were brought to my office and later taken over to some other office. A general audit and accounting of the books was made and a written report prepared. I informed Mr. McDevitt orally on or about May 19, 1921, of a partial result of our investigation of the books, telling him in substance that we had determined that there were trust receipts at the plaintiff bank, but the collateral was not in the bank and was not in the safe of the Cotton Company, and that we had been unable to find such collateral. We had completed our examination of the books and found that the moneys had not been checked from the checking account to cover the collateral on those trust receipts, and we had not completely audited the books and did not make a written report at that time, but this much we had ascertained and that I communicated to Mr. McDevitt orally. This is the first information I gave Mr. McDevitt. In conducting that investigation it became necessary for me to send letters outside the State of California to obtain certain data and information. Later the written reports were prepared bear-



(Testimony of R. W. E. Cole.)

ing date July 15 and July 16, 1921, respectively, and were delivered to Mr. McDevitt at or about these dates. The first report deals with the items covered by plaintiff's second cause of action. Whereupon the written reports so prepared by Mr. Cole, auditor, were offered and received in evidence as plaintiff's exhibit 14, a portion of which is as follows:

Los Angeles, California, July 15, 1921.

California Cotton & Factorage Co.

934 Merchants National Bank Bldg.

Los Angeles, California.

Gentlemen:—

Attention T. W. McDevitt

We have audited the books and records of your Company and hand you, attached hereto, two schedules as follows;

J. B. Sears, Personal Account: This account shows in detail all debits and credits passed to Mr. Sears' account. There is an overdraft of \$5,503.88. This schedule is accompanied by all original paid bank checks and copies of journal vouchers supporting the debits to his account.

Schedule of Accepted Drafts due the Citizens National Bank: The unpaid accepted drafts amount to \$82,487.96. The collateral of 1476 bales, compress or yard receipts, has been removed from the Bank and Trust Receipts given in their place. These Trust Receipts were signed by California Cotton & Factorage Co. by J. B. Sears, Manager. Audit of these compress or yard receipts on hand as of April 30th, 1921



(Testimony of R. W. E. Cole.)

reveals the fact that of the above 1476 bales only 385 were on hand on that date.

The receipts on hand, 385 had been collat-

eral for		\$21,859.24
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Those not on hand 1,091 had been collat-

eral for		\$60,628.72
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Total	1,476 Bales Cotton	\$82,487.96
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Respectfully submitted,

R. W. E. COLE

JSB

Certified Public Accountant

CALIFORNIA COTTON & FACTORAGE CO.  
SCHEDULE OF ACCEPTED DRAFTS

DUE

CITIZENS NATIONAL BANK

APRIL 30, 1921

Date of Draft 1920.	Drawer	Accepted 1920	Amount	Payee	Number of		
					Bales Cotton.	Trust Receipt Deposited by J. B. Sears	
Nov. 18	Calexico National Bank	Nov. 19	\$ 2,675.25	Calexico National Bank	25	77	
Nov. 16	T. W. Ewing	Nov. 20	366.81	E. G. Carruthers State Bank	4	78	
Nov. 17	W. T. Carruth	Nov. 22	2,293.60	R. G. Warren	21	79	
Nov. 17	W. T. Carruth	Nov. 22	2,632.20	R. G. Warren	34	80	
Nov. 18	W. T. Carruth	Nov. 22	4,197.99	R. G. Warren	52	81	
Nov. 20	Orcutt Pawley	Nov. 22	465.65	Yuma National Bank	7	82	
Nov. 18	T. W. Ewing	Nov. 22	995.27	E. G. Carruthers State Bank	14	83	
Nov. 20	W. T. Carruth	Nov. 23	412.46	R. G. Warren	5	84	
Nov. 20	W. T. Carruth	Nov. 23	443.65	R. G. Warren	5	85	
Nov. 19	W. T. Carruth	Nov. 23	141.23	R. G. Warren	2	86	
Nov. 19	W. T. Carruth	Nov. 22	2,455.25	R. G. Warren	35	87	
Nov. 20	W. T. Carruth	Nov. 23	1,502.11	R. G. Warren	25	88	
Nov. 20	T. W. Ewing	Nov. 24	522.43	E. G. Carruthers State Bank	7	89	

Nov. 24	Orcutt Pawley	Nov. 26	331.44	Yuma National Bank	5	90
Nov. 22	W. T. Carruth	Nov. 26	1,414.13	R. G. Warren	23	91
Nov. 22	W. T. Carruth	Nov. 27	395.16	Hellman Comm'l T & S Bank	7	92
Nov. 23	W. T. Carruth	Nov. 27	3,208.94	Jack McDaniels	50	93
Nov. 23	W. T. Carruth	Nov. 27	284.16	R. G. Warren	5	94
Nov. 26	Orcutt Pawley	Nov. 29	2,270.16	Yuma National Bank	35	95
Nov. 23	T. W. Ewing	Nov. 29	130.70	E. G. Caruthers State Bank	2	96
Nov. 30	W. F. Reeves	Nov. 30	293.00	W. F. Reeves	7	97
Nov. 26	W. T. Carruth	Nov. 30	62.47	Hellman Comm'l T. & S. Bank	1	98
Nov. 26	W. T. Carruth	Nov. 30	1,352.57	Jack McDaniels	23	99
Nov. 27	W. T. Carruth	Nov. 30	263.23	R. G. Warren	6	100
Nov. 27	W. T. Carruth	Nov. 30	248.23	R. G. Warren	4	101
Nov. 29	Orcutt Pawley	Dec. 1	922.46	Yuma National Bank	15	102
Nov. 29	W. T. Carruth	Dec. 2	1,445.58	R. G. Warren	27	103
Dec. 1	W. T. Carruth	Dec. 4	855.47	R. G. Warren	17	104
Dec. 2	Orcutt Pawley	Dec. 6	676.70	Yuma National Bank	11	105
Dec. 4	Orcutt Pawley	Dec. 7	367.01	Yuma National Bank	6	106
Dec. 6	Calexico National Bank	Dec. 7	6,913.98	Calexico National Bank	76	107
Dec. 4	W. T. Carruth	Dec. 8	1,006.58	Hellman Comm'l T & S Bank	18	108
Dec. 4	W. T. Carruth	Dec. 8	640.74	R. G. Warren	11	109
Dec. 4	W. T. Carruth	Dec. 8	313.45	R. G. Warren	5	110
Dec. 6	S. M. Walker	Dec. 9	117.27	Burton & Williams	2	111

Dec. 4	T. W. Ewing	Dec. 9	778.18	E. G. Caruthers State Bank	12	112
Dec. 6	W. T. Carruth	Dec. 9	605.13	R. G. Warren	10	113
Dec. 8	Orcutt Pawley	Dec. 10	1,783.31	Yuma National Bank	26	114
Dec. 6	T. W. Ewing	Dec. 10	186.65	E. G. Caruthers State Bank	3	115
Dec. 7	T. W. Ewing	Dec. 11	142.49	E. G. Caruthers State Bank	2	116
Dec. 9	Orcutt Pawley	Dec. 13	887.88	Yuma National Bank	14	117
Dec. 9	T. W. Ewing	Dec. 14	128.69	E. G. Caruthers State Bank	2	118
Dec. 15	Calexico National Bank	Dec. 16	8,664.82	Calexico National Bank	89	119
Dec. 13	W. T. Carruth	Dec. 16	589.05	R. G. Warren	10	120
Dec. 13	W. T. Carruth	Dec. 16	186.58	R. G. Warren	3	121
Dec. 15	Orcutt Pawley	Dec. 16	181.30	Yuma National Bank	3	122
Dec. 14	W. T. Carruth	Dec. 17	1,073.90	R. G. Warren	20	123
Sub-total			57,825.31		786	

Schedule of Accepted Drafts—2

Date of Draft 1920	Drawer	Accepted 1920	Amount	Payee	Number of Bales Cotton.	Number of Trust Receipt Deposited by J. B. Sears.
Amounts Brought Forward			\$57,825.31		786	



Dec. 20	W. T. Carruth	Dec. 23	217.01	R. G. Warren	4	124
Dec. 20	W. T. Carruth	Dec. 23	1,079.56	R. G. Warren	25	125
Dec. 24	W. T. Carruth	Dec. 28	285.70	Hellman Comm'l T & S Bank	5	126
1921						
Jan. 8	W. T. Carruth	Jan. 11	478.29	R. G. Warren	10	127
Jan. 10	Orcutt Pawley	Jan. 13	296.17	Yuma National Bank	5	128
Jan. 10	W. T. Carruth	Jan. 14	585.09	Hellman Comm'l T & S Bank	10	129
Jan. 15	W. T. Carruth	Jan. 18	817.60	R. G. Warren	15	130
Jan. 18	Mrs. M. Ida Reeves	Jan. 18	254.20	Mrs. M. Ida Reeves	5	131
Jan. 24	Bert P. Snell	Jan. 25	2,000.00	Wm. Loftus, Treasurer	52	132
Jan. 28	W. T. Carruth		301.81	R. G. Warren	5	133
Jan. 28	W. T. Carruth	Feb. 1	201.05	Hellman Comm'l T & S Bank	4	134
Jan. 31	Orcutt Pawley	Feb. 1	2,570.70	Yuma National Bank	37	135
Feb. 1	W. T. Carruth	Feb. 4	258.27	R. G. Warren	5	136
Jan. 31	Orcutt Pawley	Feb. 4	264.00	Yuma National Bank	13	137
Feb. 1	Orcutt Pawley	Feb. 4	45.48	Yuma National Bank	2	138
Feb. 1	Orcutt Pawley	Feb. 4	931.71	Yuma National Bank	13	139
Jan. 31	Orcutt Pawley	Feb. 4	45.40	Yuma National Bank	1	140
Feb. 2	W. T. Carruth	Feb. 7	400.19	R. G. Warren	10	141
Feb. 2	W. T. Carruth	Feb. 7	527.89	R. G. Warren	10	142
Feb. 5	W. T. Carruth	Feb. 8	43.90	Hellman Comm'l T & S Bank	1	143
Feb. 2	W. T. Carruth	Feb. 8	284.42	Jack McDaniels	5	144

Feb. 4	W. T. Carruth	Feb. 8	254.61	Jack McDaniels	5	145
Feb. 8	W. T. Carruth	Feb. 10	527.12	R. G. Warren	10	146
Feb. 15	W. T. Carruth	Feb. 19	754.65	R. G. Warren	15	147
Feb. 15	W. T. Carruth	Feb. 19	256.06	R. G. Warren	5	148
Feb. 15	W. T. Carruth	Feb. 19	405.77	R. G. Warren	10	149
Feb. 19	W. T. Carruth	Feb. 25	214.85	Hellman Comm'l T & S Bank	5	150
Mar. 4	Orcutt Pawley	Mar. 5	898.16	Yuma National Bank	39	151
Mar. 9	W. T. Carruth	Mar. 14	387.51	R. G. Warren	11	152
Mar. 14	First National Bank Calxico	Mar. 15	1,920.00	First National Bank Calxico	20	153
Mar. 22	W. T. Carruth	Mar. 25	168.28	R. G. Warren	5	154
Mar. 24	W. T. Carruth	Mar. 28	318.16	R. G. Warren	8	155
Mar. 26	Orcutt Pawley	Apr. 2	1,261.20	Yuma National Bank	41	157
Mar. 31	Orcutt Pawley	Apr. 4	2,005.70	Yuma National Bank	92	158
Apr. 8	R. G. Warren	Apr. 12	822.50	R. G. Warren	22	159
Apr. 12	First National Bank, Calxico	Apr. 13	392.00	First National Bank Calxico	65	160
Apr. 22	South West Cotton Co.	Apr. 25	1,134.36	South West Cotton Co.	52	161
Apr. 22	South West Cotton Co.	Apr. 25	1,053.28	South West Cotton Co.	48	162
Totals			<u>\$82,487.96</u>		<u>1,476</u>	

The above schedule of Accepted Drafts were unpaid on April 30th, 1921. The compress or yard receipts accompanying these drafts, and originally held by the Citizens National Bank as collateral security, have in each case been replaced by a Trust Receipt similar in form to the sample attached hereto and signed by California Cotton & Factorage Co., by J. B. Sears, Manager.

(Testimony of L. O. Ivey.)

The witness

L. O. IVEY,

a witness on behalf of plaintiff, was recalled.

#### FURTHER DIRECT EXAMINATION

The witness produced and there was furnished to counsel for defendant the ledger sheet of the bank showing the account of the California Cotton and Factorage Company. Of the 1476 cotton tickets covered by the 87 trust receipts held by the plaintiff bank at the date of Mr. Sears' death, 385 were returned to the bank. They could not be segregated so as to determine to which particular acceptance, if any, they belonged. The plaintiff bank sold the 385 cotton tickets and realized therefor \$14,727.54, which money is being held by the plaintiff bank in the form of a cashier's check and has not been allocated to any particular account, awaiting the outcome of this litigation. It was thereupon stipulated that all of the cotton tickets which were received at the plaintiff bank and by it turned over to the Cotton Company in lieu of the trust receipts were negotiable by delivery, and their value and effect were substantially the same as a warehouse receipt. All of the 87 sight drafts which were drawn through the plaintiff bank upon the Cotton Company and accepted by the Cotton Company, were paid by the plaintiff bank and after payment were carried by the bank as bills receivable and were in charge of the note department of the bank. There are three note-tellers in the note department and a party who desires



(Testimony of J. S. Bailey.)

to pay a note goes to the window of the note department and pays his money to one of the tellers at the window. Although I was in charge of the note department I do not pretend to know every time a note is paid or who pays it or the manner in which it is paid, as the details are attended to by the note-tellers.

Whereupon the witness was withdrawn from the stand to be returned later for further examination.

Whereupon

J. S. BAILEY,

a witness on behalf of plaintiff, being duly sworn, testified.

#### DIRECT EXAMINATION

I reside in Los Angeles and am a public accountant, not certified, and have been practising that profession for four years. I was associated with R. W. E. Cole in April, May, June and July of 1921. I was acquainted with J. B. Sears prior to his death, meeting him in the office of the Cotton Company in relation to another audit that was being carried on and of which his office had some information. That audit had nothing to do with this case. On April 30, 1921, I was present in Mr. Cole's office when Mr. McDevitt employed Mr. Cole to audit the books of the Cotton Company, and I went with Mr. McDevitt to the Cotton Company's office to get the records for that purpose. Mr. McDevitt instructed Mr. Collins and Mr. Norsworthy that I would take charge of the Cotton Com-

(Testimony of J. S. Bailey.)

pany's office and that they should render me any assistance which they could in the matter of making an audit. I made an audit of the books commencing Saturday, April 30, and ending May 19, 1921. On the latter date I made a report to Mr. Cole.

In the making of the audit I did not find in any book of the Cotton Company any entry showing the issuance of trust receipts, although I examined carefully all the books and records that were turned into my possession. The witness' attention was called to the book of the Cotton Company marked "Check Stub Register", and particularly the page headed "Acceptances, The Citizens National Bank, Los Angeles", and the witness identified such account as being that in which was listed the sight drafts which had been accepted by the Cotton Company during the second season of its operation. It was not an acceptance account—the acceptance account is in the ledger. It was just a list of acceptances. In the first column is set forth the number in numerical as well as chronological order which the draft bore and the date appearing thereon is the date of the acceptance, that is, the date on which the sight draft was accepted, and the next column shows that the draft was drawn through the Citizens National Bank; and the next column shows that the particular draft in question was drawn by the Southwest Cotton Company of Yuma and covered 61 bales of Krabos cotton weighing 31,626 pounds. Krabos is a grade of cotton. Whereupon the witness was referred to the acceptance bearing

(Testimony of J. S. Bailey.)

number 77, in the amount of \$2,675.25. The witness thereupon identified said acceptance as being the sight draft dated November 18, 1920, being a portion of plaintiff's exhibit number 6 and identified the amount of the sight draft with the amount inserted in the acceptance account. The letters L. F. appearing in still another column indicate "ledger folio", and a reference to the ledger folio page as indicated in the list of acceptances shows that the ledger of the Cotton Company reflects that acceptance number 77, in the amount of \$2,675.25, was paid. The next column on the ledger under the heading "Straight Cotton, Bales" indicates the number of bales, and in connection with acceptance number 77 shows 25 bales, which corresponds with the entry on the acceptance. I have checked through all of the 87 acceptances with the entries in the acceptance list, and find that the same procedure was followed in the making of entries in the Cotton Company's books covering each and every acceptance, and I found that each acceptance was given a number and that the numbers are in consecutive order, and there should have been an entry in the ledger account of the Citizens National Bank reflecting the transaction. Whereupon the witness' attention was directed to page 38 of the Cotton Company's ledger and the account entitled "Citizens National Bank", and to the date November 19, 1920. The entry of the acceptance dated November 19, 1920, is included in an entry made November 30, 1920, covering acceptances numbers 43 to 101, it appearing that the



(Testimony of J. S. Bailey.)

ledger entries of acceptances in the account entitled "Citizens National Bank" was made once each month, and such entry gave the numbers of the acceptances and the total amount. The manner in which the Cotton Company's books were kept shows that when a sight draft was accepted by the Cotton Company it made a credit entry in the said acceptance account of the "Citizens National Bank", and when the Cotton Company paid off these acceptances they made a debit entry. The procedure in accounting is to use the "credit entry" for registering a liability, and for decreasing the liability a "debit entry" would offset that amount, and so when the Cotton Company made a "credit entry" upon its books it showed they owed the plaintiff bank that amount of money, and when they made a "debit entry" it decreased the indebtedness by that amount. The account headed acceptances in the check stub register of the Cotton Company shows that all of the acceptances up to 76 were paid, and that also number 156 was paid, but that numbers 77 to 155, inclusive, were not paid. It ought to set up some other account as a liability, but the reference there, p. 40, is a correct reference which is traceable to page 40 of this acceptance account, but I think it ought to appear elsewhere. It shows that acceptance number 76 was paid on March 25, 1921, on which date acceptances numbers 73, 74 and 75 were also paid, in the aggregate sum of \$12,854.41. A reference to the bank book of the Cotton Company discloses that during the month of March there was not entered in the pass book of the Cotton Company any credit in the



(Testimony of J. S. Bailey.)

sum of \$12,854.41. The witness then referred to the "check register" of the Cotton Company, and referred to Check No. 1389, dated March 25, 1921, drawn in favor of the plaintiff bank in the sum of \$12,854.41, and which book shows that said check covers four acceptances. It was then stipulated by counsel that the payment of acceptances by check of the Cotton Company was not made concurrent with the deposit of outbound drafts covering cotton sold, but said payments were made on acceptances from time to time as money was available in the checking account of the Cotton Company.

I found in the vault of the Cotton Company after Mr. Sears' death, 385 cotton tickets that belonged to the plaintiff bank. There were also in the safe of the Cotton Company some cotton tickets not covered by trust receipts in favor of the bank. I did not find anything in the books of the Cotton Company which would indicate that the cotton tickets on hand were covered by trust receipts. I knew that there were trust receipts outstanding, because I had previously been over to the plaintiff bank and checked up the acceptances and I noticed that the trust receipts were attached to all of the acceptances in the place of the collateral which had been taken away. It is the custom of accountants in checking up liabilities such as acceptances to go to the one who holds the acceptances and check them up with the books of the company to see that they are correct, and I did this in this case. It was then that I discovered that these

(Testimony of J. S. Bailey.)

acceptances had attached to them trust receipts instead of the collateral.

Whereupon there was exhibited to the witness plaintiff's exhibit 14, certain portions of which he identified as a trial balance of the books of the Cotton Company as of April 30, 1921. Such trial balance does not show any trust account. The audit prepared by me reflects the account of J. B. Sears with the Cotton Company as shown in its books. The report prepared by me of the personal account of J. B. Sears shows credits against his account of \$11,794.49 and debits of \$17,298.37, the difference being a debit charged against his account of \$5,503.88, that is, he had drawn that much more money from the Company's funds than he put back. The detail of the withdrawals and deposits is shown in the report. The report shows in detail the number of each check charged against his account. It was stipulated that the charge of \$27.39, evidenced by check of May 5, 1921, is not a proper charge *charge* the account of Sears and should not be taken into consideration.

I did not in my examination of the books and accounts of the Cotton Company find any entry or memorandum showing the issuance of trust receipts to the plaintiff bank and the taking up of the cotton tickets that were attached to the acceptances. Likewise I found no record in the books and accounts of the Cotton Company showing that the 385 cotton tickets found in the safe of the Cotton Company had been received by the Company in exchange for trust receipts.

(Testimony of J. S. Bailey.)

The ledger of the Cotton Company carries an entry corresponding to each of the entries in the bank pass book of the Cotton Company. The deposits were posted in the ledger to the current checking account and is shown on page 34 of the ledger. I have checked the ledger and deposit book and find that the entries correspond all the way through, both as to amount and date of deposit.

“Q Now is there any entry or memorandum that you were able to find in any of the books or accounts of the California Cotton and Factorage Company which showed or indicated to you that the amount of money entered in the bank book or entered into the ledger in the Citizens National Bank account, the cash account of the Citizens National Bank,—that the money was received from the sale of cotton against which there were outstanding trust certificates? Do you understand the question?

A Yes, sir. The entry wouldn't show that way without investigating it. On the face of it it would not appear. It appears as proceeds of the sale of cotton. Now to determine anything about that cotton you would have to go further to investigate and see what cotton it was.

Q Now how could you do that?

A The sale number would be indicated in connection with the money received and deposited, the sight draft drawn and deposited; then you would have to refer to the sales invoice—

Q What is a sales invoice?



(Testimony of J. S. Bailey.)

A A sales invoice is an invoice of the cotton sold indicating the number of bales and the bale tickets and the grade and the terms of sale.

Q And that invoice is, as invoices are generally understood to be, a sheet of paper about 10 x 10, is it?

A Yes.

Q A loose sheet of paper?

A Yes.

Q And what other accounting procedure would you follow in order to run the thing down?

A To run it down, you would have to trace each bale number. You would take the bale numbers on the invoices and run down the bale and see the source of it to determine what cotton it was."

The trust receipts contained no bale numbers, and from an examination of the trust receipt or of an acceptance you could not tell what bales were covered thereby, but only the number of bales. I found among the records of the Cotton Company sheets known as "buyers' reports", being reports filled out by the buyer in the field informing the office of the Cotton Company in Los Angeles that he had purchased a certain number of bales of cotton, giving the numbers of the bales, that he enclosed with the draft which was issued to pay for the cotton. From this "buyers' report" I was able to associate the number of the acceptance and the amount of the acceptance and the particular acceptance with particular bales of cotton covered thereby.



(Testimony of J. S. Bailey.)

### CROSS EXAMINATION

I was able without difficulty to trace the receipt and expenditure of all money which went into the bank, and the books of the Cotton Company were complete so far as reflecting the receipt and disbursement of moneys, and with regard to cash is a fairly complete set of books. It is a double-entry system of bookkeeping and was comprehensive enough to handle this kind of business so far as it went. At the time I examined the books I had some difficulty in arriving at the true financial condition of the Company because the books did not register all of the assets or liabilities and it was necessary to determine what they were before I could arrive at the financial condition of the company. They did not reflect a special deposit in the bank of \$26,000.00 and there were a number of loans to Chinese ranchers in Lower California that were not shown as notes or accounts receivable. The furniture and fixture account was understated in that it was carried on the books at \$5.00. I believe that is all the assets that I found not entered. The liability to the Citizens National Bank for notes payable for these cotton loans was not reflected in the books. In the books I examined I found no record either of the credits or debits regarding these special loans. There was no liability recorded in the books for the issuance of the trust receipts to the plaintiff bank. That was a liability in addition to the acceptance account. The books did show, however, fully and fairly, the number and amount of each acceptance which the bank paid for

(Testimony of J. S. Bailey.)

the Cotton Company, and by looking at the books you can find out at any time how many acceptances were held by the plaintiff bank on which the Cotton Company was liable, and the books show that on April 30, 1921, there were 87 of these acceptances unpaid; all of which were registered in the books of the Cotton Company as moneys due and owing from the Cotton Company to the bank. These acceptances were referred to in the "acceptance account", as well as in the "Citizens National Bank account", as set up in the ledger. It is summarized in the ledger and itemized in the acceptance book, and the total amount of the acceptances unpaid at the termination of business on April 30, 1921, was approximately \$82,000.00. To each of these acceptances there was attached trust receipts covering the cotton tickets delivered by the bank to the Cotton Company.

"Q What entry would you have made in the books showing a liability of the Cotton Company to the bank except the entry of the \$82,000.00 which is already entered?

MR. COSGROVE: You mean what entry would have been made after the bank had surrendered the cotton and taken the trust receipt, then?

MR. PARKE: Yes.

MR. COSGROVE: All right, no objection.

A From an accounting standpoint, the liability for the return of the collateral was an independent and separate liability of the California Cotton and Factorage Company.

(Testimony of J. S. Bailey.)

Q BY MR. PARKE: That is merely from an accountant's standpoint, is it not?

A Yes.

Q But for practical purposes the same indebtedness evidenced by the acceptance account would be duplicated by this entry of the trust account, would it not?

THE COURT: Well, he is asked in substance, as I understand it, as to whether or not that would be a duplication of accounts, as an accountant.

MR. PARKE: That is right.

THE COURT: Would it?

A It would not, no."

The books indicate that the Cotton Company owed the Citizens National Bank \$82,000.00 on certain acceptances unpaid for which the bank was holding as collateral trust receipts evidencing approximately 1400 cotton tickets. In making up the trust account I would have set up in the books a liability for the trust receipts, or some such title as that, and would have entered therein a credit to the trust account indicating there was a liability of the Cotton Company to the Citizens National Bank for the return of certain collateral, making the amount of such credit the same amount for which the cotton tickets were originally held as collateral.

"Q In other words, if an acceptance came to the Citizens National Bank, we will say on September 30, for \$8,000.00, to which was pinned ten tickets, and the Cotton Company accepted the acceptance, the draft, and then took the tickets and gave a trust receipt, you

(Testimony of J. S. Bailey.)

would enter as a credit there the \$8,000.00, being the same amount as the acceptance, would you not?

A Yes, sir.

Q So that that indebtedness, then, would duplicate a like entry made in the acceptance record, would it not?

A It is duplicated only in the amount of money, but not in the nature of the entry.

Q It would be duplicated in the amount of money, would it not?

A Yes.

Q So that the total number of tickets you would enter in your trust account for the cotton tickets which the Cotton Company had received would, in amount, be identical with the like entries in the acceptance account?

A If the tickets had all been taken away and trust receipts given for the same list.

Q Yes. In those cases where trust receipts were taken for the acceptances then the amount would be the same?

A The same yes.

Q So that, assuming, as the evidence shows in this case, that attached to those 87 drafts were approximately 1,400 cotton tickets, and trust receipts substituted, the total amount of entries which you would have put on the credit side of the trust account would have aggregated the total amount of the face of the acceptances?



(Testimony of J. S. Bailey.)

A If trust receipts were attached to all of them, yes."

Q And what would you have entered on the charge side of this trust account?

A Cotton entries.

Q But what figures; what numerical entry?

A The same amount of money.

Q Would you have had a total entry there of credits and debits each in identical figures?

A In this particular case it would have turned out that way.

Q When would you have made those entries on the deposit?

A At the same time you make the entry on the credit side.

Q How could you then have ascertained when the indebtedness, as you say, due from the Cotton Company to the bank had been paid; that is, when had the tickets been returned?

A When the tickets were returned then I would reverse the entry and extinguish the liability.

Q Well, I always have it reversed. So that you would have charged the Cotton Company with the receipt of these cotton tickets at the value evidenced by the acceptance to which they were attached?

A Yes.

Q And then as they took up these trust receipts you would have credited the Cotton Company with that amount; is that correct?

A Well, you have the debits and credits reversed.

(Testimony of J. S. Bailey.)

Q Well, I appreciate that. But I think you mean just what I do. So that at all times the amount of money reflected in your trust account as owing by the Cotton Company to the bank would be the same as is reflected in the acceptance account, assuming that each acceptance had tickets attached and trust receipts substituted?

A Would be the same, yes."

Sometimes, not frequently, if you have any doubt as to the existence of liabilities which are not in view it is necessary in order to check the books of the particular institution you are auditing to go to the bank with which the institution does business to check the data there, the bank data supplementing that of the records as disclosed in the books of the company. In this case I was able without difficulty, at first glance, to see that the Cotton Company was buying cotton on acceptances through the plaintiff bank, and that it was making payments to the bank from time to time by checks drawn on its checking account, and that the Cotton Company was taking the cotton tickets from the bank and issuing trust receipts in lieu thereof. There was no concealment of that fact and it is easily ascertainable by an examination of the acceptances at the bank.

This is the first Cotton Company that I ever audited. I am familiar with what is familiarly known as "bill of lading account", under which it is customary to have the bank pay for the drafts and then the customer goes to the bank and gets the evidence of own-

(Testimony of J. S. Bailey.)

ership of the property purchased, sells it, and gets the bill of lading and redeposits it in the bank. I understood that was the way in which the Cotton Company handled its affairs, and that is the customary way of brokerage concerns handling materials, where they buy it in the field and then sell it in the open market.

I found among the books of the Cotton Company a book designated as "class book", wherein cotton purchased by the Cotton Company was entered in various classes as to grades and so forth, but I did not examine the book. This book was in the safe the last day I saw the books.

I ascertained that the 324 tickets I found in the safe belonged to the acceptances held by the plaintiff bank by first getting together all the "buyers' reports" and making a list of the bale numbers. Then I found the particular draft that covered the purchase of certain cotton, so that I was able to identify certain bale numbers with certain drafts. Then when I found 385 tickets in the safe, by comparing the bale numbers with the "buyers' reports" in the field I was enabled thereby to connect it up with the acceptances in the bank. By checking back from the "buyers' reports" I was able to go to the bank and see the acceptance which was drawn by the party from whom the cotton was purchased, as shown in such "buyers' report", and was thus able by putting the "buyers' report" with the acceptance to easily ascertain which particular bales of cotton, by individual bale numbers, belonged to the particular acceptance. I found a great many "buyers' re-



(Testimony of J. S. Bailey.)

ports" among the files of the Company and they constituted a part of the records of the Company. From these "buyers' reports" I was able to ascertain what particular cotton was purchased by any particular acceptance. I also found among the Cotton Company's records, reports of sales of cotton. I checked up to see what became of the approximately 1,000 cotton tickets that were covered by trust receipts held by the bank, and which the Cotton Company had sold and disposed of, and with the exception of a few instances I was able from the records and books of the Cotton Company to trace the disposition of all the cotton so sold and disposed of by its identical bale number. I found that each and all of the cotton tickets which were covered by trust receipts held by the bank and for which cotton tickets were not found in the safe, had been disposed of by the Cotton Company. I am not sure about the description of the funds that were deposited. I know the amount of the sale was deposited in the checking account.

"Q Now referring back again to your trust account, supposing that after the Cotton Company had gone to the bank and secured, we will say, a hundred tickets evidencing a hundred bales of cotton and had given trust receipts therefor, there was a fall or decline in the cotton market so that the value of that ten bales of cotton depreciated from \$5,000.00 to \$3,000.00, would you make a corresponding entry in your trust account?



(Testimony of J. S. Bailey.)

A The trust account would have to check out, and to do that you would have an adjustment account to take care of any shrinkage in the dollars and cents.

Q Oh, you would still have another account, then, to take care of that?

A If that contingency arose, yes.

Q What?

A If it was necessary you would have an adjustment account to take care of shrinkage.

Q And would it be necessary?

A It would be necessary until the liability had been taken up, then the whole thing would clear up, and if the liabilities were all taken up there would be no such account left on the books.

Q But assuming that before the liabilities were all taken up, and while the Cotton Company still has unpaid a great many trust receipts or acceptances, they should call for the return of the cotton tickets, what would measure the Cotton Company's liability—would it be the then value of the cotton tickets or the initial cost of those cotton tickets as evidenced by the acceptances?

THE COURT: You say if they should call for the return of the cotton tickets, who?

MR. PARKE: The bank.

Q Would it not be necessary to reflect in your trust account, from day to day, the value of those cotton tickets?

A Yes; the value of the tickets themselves would be measured by the daily market.

(Testimony of J. S. Bailey.)

Q Now this trust account you speak of as being necessary is one which would reflect the responsibility of the Cotton Company to the bank for these cotton tickets which had been entrusted to it?

A Yes.

Q Now I again ask you, would you have the trust account, therefore, reflect the daily value of those tickets which were held in trust, or would you have it reflect the initial cost of those tickets?

A No; that would be the same thing.

Q So that you would not, then, keep the trust account in the manner you first indicated, would you?

A On any particular date, if you wanted to find a particular condition on any definite date, the trust tickets would have to be valued by the market value of the cotton on that day.

Q And it would necessitate a very comprehensive set of accounts, would it not, to keep an exact record of the value and adjust the value of those cotton tickets every day?

A No, no more comprehensive than is used in a stock broker's office for valuing shorts. The same principle.

Q Well, this would be necessary, would it not, when the cotton market was active to make several different entries each day as the market fluctuated?

A You would make the entries as often as you wanted to determine the condition. Not several hours a day, but once a day, or once a week, or as many times as you wanted to find out where you stood.

(Testimony of J. S. Bailey.)

Q And each cotton ticket valuation would have to be changed according to its grade and its fluctuation on the market each day?

A To make it exact, yes, you would have to bring it down to the grades.

My recollection is that I saw among the books of the Cotton Company a book wherein was entered the grading or classing of cotton, wherein was listed the cotton on hand, classifying it as to grades, or kept for that purpose, although it didn't carry out the effect. I examined the book carefully. From that book I could tell how much cotton should be on hand by subtracting the cotton sold from the cotton bought, but that book would not tell whether any one had a lien against the cotton; That there was a lien evidenced by trust receipts would have to be ascertained by going outside the books of the Cotton Company. It is not unusual, however, that auditors have to go outside the books of the Company to ascertain its true financial condition.

Regarding the portion of my report in relation to Mr. Sears' personal account, I know nothing regarding any of the various transactions, except such as I got from the books and records of the Cotton Company, and particularly from the checks themselves and from the journal entries. There were three or four journal entries and the rest of those were checking items. A journal entry is merely a non cash transaction that is used to transfer it without a transfer of cash. When there is a check drawn it appears as a



(Testimony of J. S. Bailey.)

check entry. There was a petty cash book kept. If any of these expenditures came from the petty cash there would be a description of it in there. Or if it came through the journal the explanation as to what the money was paid out for would in some cases follow the journal entry. The entry as to the petty cash items would not necessarily indicate the expenditure but the disposition of the charge. Where there was a journal entry the purpose for which the expenditure was made would not be indicated. If there was cash paid out for some one's personal account it did not show the purpose of it but merely disclosed the disposition of the charge. If it was for salary or for expenses it would so state, but if it was for some personal matter it would not necessarily give the explanation.

Referring to the first item of \$1000.00, the entry of \$1000.00 appears on page 5 of the journal. It says 'September 11, 1919, debit J. B. Sears and credit McFadden Agency \$1000.00.' That is the only explanation there is of that item. As to the next item, Check No. 1, being check entry No. 1, the check register starts with check No. 8. The first seven checks were evidently covered by a journal entry somewhere. I would not be able to say offhand just how that was arrived at.

Referring to the next check No. 35, dated October 16, 1919, an entry is made in this check register without page 'check No. 35, October 16, J. B. Sears' personal account—\$50.00.' The entry clearly reflects that



(Testimony of J. S. Bailey.)

it was drawn for Mr. Sears' personal account, and the check does also. It says personal account down in the corner. The signature is Mr. Sears' handwriting. I don't know whose handwriting the item personal account is. I find practically all the checks drawn to J. B. Sears a clear, unconcealed purpose for which it was issued, and the checks drawn to Mr. Sears personally as payee which does not include the distribution of the ones which I found proper entries in the books.

Referring to check No. 2 dated September 12, 1919, in favor of Bishop and Bailey in the amount of \$130.70 which I have charged to Mr. Sears' personal account, this check is one of the first seven and I don't know just where to find these entries here. There is nothing on that check to indicate. There is nothing on check No. 5 likewise payable to Bishop and Bailey, in the amount of 90¢, to indicate that it should be properly chargeable to Sears' personal account.

I will ascertain if there is any journal entry to indicate why I allocated those two checks to Sears' personal account.

Referring to check No. 77, Menga and Morey, for \$163.85, there is nothing on that check to indicate that it was properly chargeable to J. B. Sears, but the entry in the book is "Check No. 77, November 7—J. B. Sears account—\$163.85." That entry is in Mr. Norsworthy's handwriting. Mr. Norsworthy gave me information regarding these matters during the audit. I do not remember specific instances of asking Mr. Norsworthy regarding these personal charges which I made

(Testimony of J. S. Bailey.)

to Mr. Sears, but he was around there, available, and if there was anything in which he could help me I felt at liberty to ask him.

Regarding the payee of that check, Menga and Morey, my recollection is from hearsay, either from Norsworthy or someone around the office, that it was a contractor that did some work for Mr. Sears.

Referring to the next item, a cash item, check No. 191, the entry shows 'December 20, 1919, check No. 191, cash disbursements, amount \$30.00.' Check No. 258 to the Los Angeles Athletic Club for \$16.75 is entered as follows: 'Check No. 258, January 7, 1920, L. A. Athletic Club dues to March 1, 1920, J. B. Sears, \$16.75.'

Touching the series of checks issued in the name of C. A. Anderson, particularly referring to check No. 411 dated March 5, 1920, for \$48.00, the entry in the book is 'Check No. 411, March 5, 1920, C. A. Anderson, account of J. B. Sears, \$48.00.' I don't know who C. A. Anderson was.

At the end of my report I gave a list of three checks, being checks No. 320, 360 and 512, which are included in this detailed statement, about which there does not appear a notation either upon the check or upon the check register that the item should be charged to Sears' account. In further instances there is a record either on the check itself or on the check register to indicate that it should be charged to Sears' account.

Giving credit to Mr. Sears, I did not make any entry for commissions of 25% due him on the operating

(Testimony of J. S. Bailey.)

profits of the company for the first year. I made no effort to compute the commissions due Mr. Sears for the first year. The book shows salary credits which I have segregated. The credits given Mr. Sears for salary do not represent merely journal entries. Mr. Sears was supposed to have \$5000.00 a year, but he was in the habit of drawing \$300.00 each month and then periodically he would make an adjustment by drawing a check for the part that he had not taken month by month, so that down in the middle of the page is an entry of 12 months at \$416.16 which would bring that from the end of the month up to where it should be. That entry was already made in the book when I found it.

MR. COSGROVE: I think we should call the witness' attention to the fact that in the account there, that \$1400.00—didn't you discover the last time you checked it—that the stenographer had gotten that over in the wrong column? Take a look at that.

A No, it was merely in the footing. It would not affect this part we are talking about.

Q Well, is not that a fact?

A Yes, it is in the wrong column as far as this exhibit is concerned; the whole thing clears out when you put it back in the column where it belongs.

The entry of \$1400.00 was part of the book record that informed me that Mr. Sears was getting \$5000.00 a year. He is credited with salary on the basis of \$5000.00 a year as shown by the books.



(Testimony of J. S. Bailey.)

Referring to check No. 173, that check was drawn to cash. In the lower left hand corner it says 'expense.' The entry is in Mr. Sears' writing, and the cash book here says, 'Check No. 173, cash, J. B. Sears,' with the posting reference to his account in the ledger of \$25.00. It is not necessarily charged to the expense account, it is charged to his personal account and his expense account is credited, no matter what he is drawing the cash for.

A few of these checks are designated in the first instance as expense account. The way I understand the situation is this: Mr. Sears would draw, as in this instance, \$25.00 to be used for him in connection with his expense. When his expense account is completed he would turn it in and his account would be credited, so necessarily the cash difference would have to be charged to him. In other words, if he wanted to take a trip to the Imperial Valley and needed, say, \$50.00 or \$75.00, he would draw a check to himself personally indicating his expense account, and then after he returned he would in turning his expense account to the company for that trip account for the money expended in that manner. The books indicate that Sears did have an expense account in additon to his salary.

I have listed checks in the sum of \$1,810.00, which I have charged against Mr. Sears in his account with the Company, all of which checks were entered in the books of the Company under the heading "J. B. Sears suspense". I can find no authority for the credit to



(Testimony of J. S. Bailey.)

Mr. Sears for these amounts by way of commission. I can find no record of where Mr. Sears was entitled to any commission.

The Company did not make an operating profit the first year. It is true that if accounts receivable, that is, the loans they made, had all been good they would have made a profit, but that is part of the operation. But aside from the bad loans, that is, excluding bills receivable, I believe the Company did make a profit the first year.

“Q In checking over the books did you find where Sears had drawn any moneys which had not been entered in the books?

MR. COSGROVE: There is no charge in the complaint that he did. I think that is without the issues.

MR. PARKE: Very well.”

I did not make any check to ascertain or compute the amount which was realized by the Cotton Company from the sale of the 1,091 cotton tickets which it had received from the Citizens National Bank and for which trust receipts were outstanding. I do not know whether the Cotton Company received the cost price of that cotton when they sold it or not.

“Q Then you do not know whether or not, if the Cotton Company had taken the proceeds from the Cotton represented by these 1,091 tickets to the acceptance window and applied the full amount received therefrom upon the acceptances, it would have paid these 87 acceptances in full?

(Testimony of J. S. Bailey.)

A I don't know that from actual investigation.

Q Did you check to ascertain whether the cotton was in any instance sold or disposed of for less than the amount which had been paid for it as evidenced by the acceptances?

A That showed up in my investigation, but I did not have that in mind in my audit.

Q But you did observe from checking sales reports through, and "buyers' reports," that the cotton was sold for less in some instances?

A Yes, sir."

I made no computation to ascertain the amount of operating loss sustained by the Cotton Company during the second years of its operations in buying and selling cotton.

"Q BY MR. PARKE: Does your report indicate or did you compute how much or the money realized by the Cotton Company from the sale of this trust cotton was used by the Cotton Company for purposes other than the payment of the acceptances?

A Well, I would be unable to state that."

The books do not indicate that the same manner of doing business as between the Cotton Company and the bank as to the manner of accepting drafts, taking cotton tickets, putting in trust receipts and payment of acceptances by checks drawn on a checking account and depositing of outbound documents in a checking account continued during the whole period of the company's operations. They show, however, that from the beginning of the fall of 1919 the Citizens National

(Testimony of J. S. Bailey.)

Bank acceptances were paid through the Citizens National Bank. That, however, was only a part of the business. Some of the acceptances came through other banks and they did not finally find their way to the Citizens National Bank. I do not know from my own information whether the same manner of accepting the drafts and the payment by the plaintiff bank obtained during the whole period of time with reference to the cotton which came through the Citizens National Bank.

During the second year of the Cotton Company's operations there were 156 drafts drawn upon the Cotton Company and accepted by it through the plaintiff bank and of that amount 77 were paid and 87 remained unpaid at the time of Mr. Sears' death. All of the 77 that were paid, were paid by checks of the Cotton Company drawn on its checking account in plaintiff bank.

#### REDIRECT EXAMINATION.

The witness' attention was directed to the six checks shown on the bottom of page 5 of plaintiff's exhibit 14, entitled "Suspense account". It was stipulated that the first check in the sum of \$800.00 was given in payment of Mr. Sears' house furniture. It was further stipulated that the \$1,810.00 represented the sixth check referred to at the bottom of page 5 of Mr. Bailey's report, the same being a part of plaintiff's exhibit 14, being the one entered under the heading "J. B. Sears' expense", represents items properly chargeable to J. B. Sears. It was thereupon stipulated many of the entries in the various books of ac-



(Testimony of Theodore West.)

count of the Cotton Company are in the handwriting of J. B. Sears. The witness thereupon identified in the "check stub register" book of the Cotton Company a large number of entries made in the handwriting of J. B. Sears, such entries appearing at various dates beginning in October of 1919 and extending up to the time of Mr. Sears' death. The number of entries so made by Mr. Sears being approximately ten per cent of the total entries. The witness also identified many entries made in the acceptance account as being in the handwriting of Mr. Sears, and the witness also identified many entries in the ledger book for the year 1920-21 as being made in the handwriting of J. B. Sears. Also like entries by J. B. Sears in the "Cash account with the Citizens National Bank". It was also stipulated that during the first year Mr. Sears made occasional entries in the various accounts of the Cotton Company.

With regard to the "buyers' reports", they showed the price at which the cotton was purchased, which price corresponded with the amount of the acceptances. These "buyers' reports" I found in a filing cabinet and in various places around the office of the Cotton Company.

#### THEODORE WEST,

witness on behalf of plaintiff, being duly sworn, testified as follows:

#### DIRECT EXAMINATION

I live in Calexico, California, and was treasurer of the California Cotton and Factorage Company from



(Testimony of Theodore West.)

the time the Company was organized. I knew J. B. Sears for ten years prior to his death. He was in charge of the Cotton Company's office during the years 1919-20 and 21. I called at the office about every two weeks, as I had other business here in Los Angeles. I am in the cotton business and have been for many years. I had a key to the Cotton Company's office. During the interval between September 1st, 1920, and the date of Mr. Sears' death I had frequent conversations with Mr. Sears respecting the business of the Cotton Company. These conferences took place nearly every time I visited the office, in the office of the California Cotton and Factorage Company. We would talk over how he was getting along. I would ask him how he was getting along and his reply was that everything was going fine. He would show me his Purchase and Sales Account, which we would go over and on one occasion he represented to be profits cotton tickets that he had in the safe. We did not discuss any books at any of these conversations, but he would go over the Purchase and Sales Account and I would want to see if his cotton was hedged. He had the cotton Purchase and Sales Account in a couple of books bound in canvas. The practice in handling cotton is to issue a compress ticket or receipt covering each individual bale of cotton. The tickets which Sears showed me were in the safe. In the late winter or early spring of 1921, Sears and I were discussing how he was coming out and he told me he was doing fine. He said "This is all profit" and reached into the

(Testimony of Theodore West.)

safe and pulled out a bunch of compress receipts, I should judge five hundred. He called them "free cotton" which means that where acceptances are in the bank covering the cotton they are all taken up and the cotton is clear—that is, you do not owe anything on it. Sears referred to the cotton tickets which he showed me as "free cotton" and said "this is all clear profit."

"Q Did Mr. Sears at any time between November 1, 1919, and May 1, 1921, inform you that he was selling cotton for which he had given the Citizens National Bank trust receipts and applying the money received from the sale of the cotton for purposes other than the satisfaction of acceptances to which the trust receipts were attached?

MR. PARKE: We object to that as calling for a conclusion of the witness. We desire to have the conversation related, if he had any conversation.

MR. COSGROVE: Well, he is going to say no. If he says yes, I will ask him what the conversation was; but the witness will say no, as I understand.

THE COURT: The objection is overruled.

MR. PARKE: May we have, for the purpose of the record, your Honor, the further objection that it is incompetent, irrelevant and immaterial, as to whether or not Mr. Sears, being delegated and in general management and control of the Company, imparted the information as to the manner in which he was disbursing funds of the Company on one particular Company account or on another particular Company account?

(Testimony of Theodore West.)

THE COURT: Of course if the general offices of the Company had notice of the irregularities they could not excuse themselves by saying that the general manager did that. I suppose it is to negative that sort of thing. The objection is overruled.

A No.

Q You say he did not.

A No sir.

Q Did you know, Mr. West, at any time between the first of November, 1920 and the first of May, 1921, that Mr. Sears was selling cotton which he had secured from the Bank and for which he had given trust receipts and was applying the proceeds from the sale to the satisfaction of indebtedness other than the indebtedness on the acceptances?

MR. PARKE: We urge the same objection that it is incompetent, irrelevant and immaterial as to whether this witness knew or did not know; and, furthermore, he is charged, being an officer of the corporation, with knowledge of the Company's affairs, as a matter of law.

THE COURT: The objection is overruled.

MR. PARKE: Exception.

A No sir."

"Q If you had known in November, 1920, and subsequent thereto, and prior to May 1, 1921, that money which Mr. Sears was using to defray the expenses in conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust



(Testimony of Theodore West.)

receipts would you have consented to his continuing the business of the Company and continuing in the capacity of secretary and general manager?

MR. PARKE: That is objected to as incompetent, irrelevant and immaterial, for the reasons heretofore stated in the objection to the other question.

THE COURT: The objection is overruled.

MR. PARKE: Exception.

A I would have notified everybody concerned and objected to the procedure.

Q BY MR. COSGROVE: You would not have consented to his continuing as general manager?

A No sir.

Q If you had known in November, 1920, and thereafter, and prior to May 1, 1921, that the money Mr. Sears was using to defray the expense of conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts would you have objected to his continuing in the position of secretary of the California Cotton & Factorage Company?

MR. PARKE: Same objection.

THE COURT: The objection is overruled.

MR. PARKE: Exception.

A Absolutely.

Q BY MR. COSGROVE: You mean you would have objected?

A Yes sir."



(Testimony of Theodore West.)

I had a discussion with Sears regarding the hedging of cotton. My purpose in checking over the Purchase & Sales Account was to see that what was not sold was hedged so that there could be no loss by the fall in the market. Mr. Sears said he had the unsold cotton hedged.

“Q Did you ever make an examination of his bank account—cash in the bank?

A No; only checked the accounts by the statements rendered by the bookkeeper.

Q Now what do you mean by that? Just explain to the Court so that the Court may know what you did in that connection.

A There was a statement rendered every month by the bookkeeper which would be sent to all of the offices—or those interested—and outside of going over the purchase and sales accounts, the books were mere routine; I simply looked at them, without considering them of any particular importance.”

I received these bookkeeper's statements each month. They were signed by Sears and attested by a notary and sent to me at Callexico by mail.

I examined those statements to see what the bank account was—that is all—just to see how it stood. I knew that Mr. Sears died on or about the 1st day of May, 1921. I should say it was about the latter part of March, or, well, sometime in March that I had my first conference with him at which I made the examinations about which I have already testified.

(Testimony of Theodore West.)

CROSS EXAMINATION

I was treasurer of the Cotton Company from its inception.

“Q And when did you resign as treasurer?

MR. COSGROVE: That is objected to on the ground that it is not the best evidence.

MR. PARKE: If he knows.

THE COURT: Yes, if he knows.

A I didn't formally resign.

Q BY MR. PARKE: Well, did you continue to discharge the duties of treasurer actively until Mr. Sears' death? A No.”

“When did you cease to be active as treasurer?

THE COURT: Fixing the time.

MR. PARKE: Yes.

A Well, in my mind, I legally ceased to be treasurer in August, 1920.

Q After August, 1920, did you do anything as treasurer?

MR. COSGROVE: We object to that as calling for a conclusion of the witness. It is a rather important matter, your Honor, as will develop here shortly, and I think the witness should be directed to state what he did in order that the Court may determine whether or not it was any deviation from what he did before or whether he did it as treasurer or in what capacity.

THE COURT: Yes; let him state.

Q BY MR. PARKE: Well, what, if anything, did you do as treasurer after August, 1920?

(Testimony of Theodore West.)

MR. COSGROVE: Now that is susceptible to the same objection.

Q BY THE COURT: What did you do acting with the corporation?

A I didn't do anything acting with the corporation after 1920.

Q BY MR. PARKE: After August, 1920?

A No."

The amount of capital stock of the Cotton Company which was issued was of the par value of \$50,000.00 and I paid in the whole \$50,000.00. I gave one share of stock each to J. P. Conduit, J. B. Sears, T. W. McDevitt, and C. H. Hartke, and the remaining 496 shares were issued to me at the time the Company was organized.

I knew Mr. Sears for about ten years before he came with the Cotton Company. He was employed by George H. McFadden & Brother and he came from that Company to the Cotton Company. I am familiar with the manner in which the McFadden Company conducted its cotton brokerage business and the ordinary routine manner in which it bought its cotton. I am a cotton broker and have been engaged in that business for about twelve years. I am acquainted with Mr. Norsworthy, bookkeeper for the Cotton Company, during the major portion of the time the Company operated. I talked with him while at the office and also with other members of the office force. I talked also with Mr. McDevitt concerning the Company's affairs.

(Testimony of Theodore West.)

“Q. Now, what books of the company, if any, did you ever examine?

A I only was interested in the purchase and sales account of the cotton.

Q Well, what particular book did you ever examine?

A The cotton account and the acceptance account.”

Thereupon the witness was shown one of the books of the Cotton Company wherein there appears an acceptance account.

“A Now this is the second season. The book I was working on was—

“Q Well, did you examine this acceptance book during the second fiscal year beginning, we will say, September 15, 1920, and thereafter?

A Not to the same extent and intensiveness as I did the first year, but enough to see whether they were making money enough to pay me. I was interested to see that, they were making money enough to pay me for my stock that I sold them, and I kept track of it on that basis.

Q Well, who pay you?

A Mr. Sears.”

It was stipulated that the same form of entries was made the first year as during the second fiscal year.

I examined also the Cotton Purchase Book—cotton bought and sold. There were two of those books and I examined both.

“Q Now take during the second year, beginning in August or September, 1920, on until Mr. Sears death,



(Testimony of Theodore West.)

and tell the Court in detail just what the nature of your examination was of those three books.

A Well, we didn't do any detailed checking, but he would show by the cotton bought and the cotton sold how many bales there would be unsold, and that he had it hedged, and that he would show by his cash account and acceptance account the number of bales on hand and that it corresponded to the acceptances in the bank. That is all the details we would go into.

Q Did you personally check the three books you have in your hand?

A Not in detail at any time, because they were always in balance. Every night the books would show how many bales of cotton had been bought and sold, and the balance on hand, and the acceptances in the bank would agree with it. If there was any difference I would want to know if they were hedged.

Q Well, did you at any time during the second year of the company's operations make any independent check for yourself of the books?

A No, nor the first year either.

Q And did you rely on the statements of Mr. Sears or upon your own investigations?

A I relied more or less on his statements, and I could see the books for myself—the totals."

Referring to a particular date in these books, take for example, March 25, 1921, you have here a total of 2564 bales of cotton bought, and you have 1971 sold. The difference is 500 and some odd bales of cotton, and the compress receipts should be the evidence.

(Testimony of Theodore West.)

Sears' acceptance account would check up with the bank and that is all we had to do, to pay the bank and Sears would have the compress receipts on hand, and I assumed that he had it hedged. I connected this information with the acceptance account, for Sears would have these tickets in the safe to show me that the Cotton Company had them all paid for. He showed me the tickets on the one occasion, as previously testified about.

It was in the latter part of the season of 1921, in March, that I talked to Mr. Sears the last time about the financial condition of the Cotton Company and he showed me the tickets in the safe and told me they were all paid for. The 1921 cotton season began in September, 1920, and ran to April, 1921. The bundle of tickets which Mr. Sears showed me were about 500. I did not at any time personally check and count the tickets. I did not at any time go to the Citizens National Bank and check the indebtedness of the Cotton Company to the bank, but took the statements as made in the office. I did not have any of these statements which were prepared monthly and mailed to me.

“Q Did you ever check or make any audit or check of the books to ascertain whether or not the statements that were being sent to you each month were correct?

A No. I never would have questioned any statements sent out by Sears.

(Testimony of Theodore West.)

Q And he, so far as you know, did have on hand at the particular date when he exhibited the tickets to you which he took from the safe, the number of tickets called for by the bought and sold cotton account?

A Yes, sir. I didn't count them, but it looked to be right.

Q Did you ever examine this ledger account wherein there appears to be an entry of cotton bought and cotton sold?

A No, not that I remember."

I knew that the Cotton Company, through Mr. Sears, was selling the cotton which it had purchased through the Citizens National Bank, and I was familiar with the way in which the Citizens National Bank handled the acceptances. I understood that the party from whom the cotton was purchased drew a draft on the Cotton Company, which draft was presented to the Cotton Company and accepted by it.

"Q And were you familiar with the manner in which the Cotton Company handled the tickets and gave trust receipts to the bank?

A Well, I am familiar with it in a general way. I don't know all the details of the transaction. But when he would make up a shipment he would go over to the bank—if they made a shipment of a hundred bales—and give a trust receipt for that hundred compress receipts, go and get a bill and send it down to the compress at Calxico, pay the charges, get a clearance and a bill of lading and put it back in the bank.



(Testimony of Theodore West.)

Q You knew, then, that the Cotton Company was securing these cotton tickets which were attached to the acceptances from the bank and giving the trust receipts?

A Yes.

Q Until they could get the shipping documents?

A Yes.

Q State whether or not, from your experience as a cotton broker, that is the usual and customary way of handling transactions of that kind.

MR. COSGROVE: We will stipulate that it is.

A It is.

MR. PARKE: In other words, that in the cotton market generally they handled it in that way?

MR. COSGROVE: Yes."

I did not know that the Cotton Company, after it sold the cotton covered by the trust receipts was selling the cotton and putting the outbound documents—that is the drafts drawn on the purchaser of the cotton together with the bill of lading therefor in the checking account of the Citizens National Bank. I thought Sears was taking up acceptances with the proceeds from the sale of the cotton covered by trust receipts. I did not know where he was depositing the money received from the sale of the cotton. I never made any check to ascertain how he was handling the monies realized from the sale of cotton.

"Q Did you ever go over, while acting as treasurer, and investigate any of the books of the Citizens Na-



(Testimony of Theodore West.)

tional Bank or any of the acceptances or records therein the bank?

A No; I never went over any records.

Q Did you ever look at the check book of the Cotton Company?

A No, I never saw a check book.

MR. COSGROVE: Do you mean by that check stubs?

MR. PARKE: Yes, the check stub book.

Q Did you ever inquire of Mr. Sears how he was paying the acceptances—that is, in what manner he was paying them?

A No, I did not."

I was familiar with the amount of cotton that was being bought by the Cotton Company and the amount that was being sold and also with the market price of cotton. Beginning in September, 1919, there was a rise in the market until about April or May of 1920, cotton going up to  $43\frac{1}{2}\phi$  for July cotton in New York and from July, 1920, to May, 1921, the cotton market went down from  $43\frac{1}{2}\phi$  to  $11\frac{1}{2}\phi$  per pound. This decrease or drop in the market was gradual. I knew that the Cotton Company was in some instances selling cotton for less than it paid for it.

"Q Had you known that Mr. Sears was handling his business in the following manner would you have objected to it: Going to the bank, getting the tickets and giving a trust receipt, then selling the cotton and taking the outbound documents, that is, the draft drawn on the purchaser of the cotton together with

(Testimony of Theodore West.)

the bill of lading, and depositing them in the general checking account of the Cotton Company at the Citizens National Bank?

A Well, I cannot answer that question yes or no. If I had known Mr. Sears was not taking acceptances when he put that money in the bank is when I would begin to kick and yell.

Q But you didn't object to the way in which he put it into the bank?

A I never did follow the details of how he did it.

Q Well, I am just asking you, though.

A No, I don't say that I would.

Q It would have been satisfactory to you had you known that he was selling the cotton and depositing the money in the way in which he did?

A Well, I don't suppose I would have objected.

THE COURT: Do you understand the question as to "the way in which he did." The witness just preceding you has said that he was expecting to take up his trust receipt first. Now the question is would you have objected if you had known that he consummated the transaction in the way in which he did. Now that, of course, carries with it the question of not first taking up the trust receipts.

MR. PARKE: I want to know of the witness whether or not his objection was as to the manner of withdrawing the funds from the general checking account or of depositing the proceeds from the sale in the general checking account.

(Testimony of Theodore West.)

THE COURT: I understand the witness, then, to mean that, assuming his trust receipts or acceptances were attended to, that you (the witness) would not have objected to this manner of depositing in the general checking account.

A No."

What I did object to was that Mr. Sears was not paying the acceptances, which fact we did not know. I expected him to pay the acceptances from the sale of cotton. I also expected him to pay the operating expenses—that is, the salaries, office expenses, etc., of the Cotton Company from the sale of cotton. I never instructed that he should not pay operating expenses out of anything except the profits and I never designated any particular fund that should be used for operating expenses. Sears issued checks out of the general fund for that purpose. I cannot say whether we had a special expense account in the bank in this particular instance or not. Mr. Sears paid the acceptances during the first year of the Company's business by checks drawn on the Company's general checking account. I do not know whether he paid operating expenses of the Cotton Company during the first year out of the general checking account or not, as I never checked the books to ascertain that fact. I considered the key to the cotton business is the Purchase and Sales Account and that is all I sat on. I know the Cotton Company had a class book wherein was listed all cotton by bale number that was purchased and all cotton by bale number that was sold,



(Testimony of Theodore West.)

but I never did look at that book. Mr. Sears, in checking the amount of cotton on hand, did not show me the number of each bale of cotton on hand, as I was not interested in that. I knew that whatever operating profit the cotton company made during the first year was written off at the end of the first season on account of bad loans. The profit consisted of 98 bales of cotton on hand and two notes, as I recollect, one given by a man by the name of Pauley and one by the McDevitt Cotton Company. The McDevitt Cotton Company loan was approximately \$30,000.00 and the loan to Pauley was approximately \$12,000.00. The net profit from the purchase and sale of cotton during the first year of the Cotton Company's business aggregated between \$50,000.00 and \$60,000.00. If the Cotton Company had during the first year sustained a loss in the purchase and sale of cotton it would have been necessary for Mr. Sears to pay operating expenses out of the capital of the Company. No arrangement was ever made by me with the plaintiff bank for an operating checking account into which profits might be put and out of which operating expenses might be charged.

I never at any time compared any of the monthly statements prepared by the bookkeeper with the books of the Cotton Company to ascertain if they were correct and I never went to the plaintiff bank to check as to the amount of cash on hand. I knew in a general way that the books that were kept by the Cotton Company were kept "cotton wise"—that is, that it had



(Testimony of Theodore West.)

a Purchase & Sales book, and Acceptance Account, a Cotton Account, and a bale book, and that they kept these books up. The books which I saw of the Cotton Company were in keeping with the usual set of books kept by cotton brokerage concerns.

The special deposit of \$25,000.00 which was opened up in the plaintiff bank in the name of "J. B. Sears Trust Account" was money originally intended to establish a bank at Gridley, California, but subsequently diverted as a guarantee or hedge for some crop loans of the Cotton Company in Calxico. That money belonged to W. J. Neale and so far as I know was never turned over to the California Cotton & Factorage Co. It was then stipulated that the plaintiff bank still hold said fund as security for those certain loans that were made.

I think the last time I was over the Cotton Company's accounts with Mr. Sears was in the latter part of March, or in April, 1921. It was on the second or fourth Thursday in April, but I cannot fix the date exactly. On that date Sears and I checked the cotton bought and sold and that is when he showed me the bunch of tickets as being clear. I estimated there were about 500 tickets and that is the amount, as I recall, that the Company's books showed should be on hand. I do not know what became of the tickets. He had to turn them in to the compress as he shipped it out, but when and how he did it, and where, I don't know, and I never made any check of the books to ascertain.

(Testimony of E. T. Pettigrew.)

E. T. PETTIGREW,

a witness called on behalf of the plaintiff, being first duly sworn, testified as follows:

I am vice president of the Citizens National Bank and have been for five or six years. I knew Mr. J. B. Sears during his life time. I saw him in the plaintiff bank.

Thereupon there was exhibited to the witness a sight draft dated April 29, 1921, drawn by the California Cotton & Factorage Co. by J. B. Sears, Manager, against the Pacific Cotton Mills Co., Inc., Alhambra, California, and his attention was directed to a pencil notation in the upper right hand corner, and the witness testified they were his initials, placed thereon so that the Cotton Company could take credit for the draft and have it go through as a cash transaction.

I do not have any independent recollection of this particular draft, but do remember that either Mr. Sears or some one from the Cotton Company would present sight drafts to the bank for O. K. or approval so that they could pass through as a cash transaction. In most cases—perhaps in all cases, there were bills of lading covering cotton attached to such sight drafts. It is not my custom to examine such documents closely. I know nothing about the cotton business. At the time I examined this particular draft. The particular draft which I have just examined discloses the number of bales of cotton and the weight and marking, etc.

(Testimony of E. T. Pettigrew.)

It was my business to see whether or not the Bill of lading attached to the sight draft covered that number of bales of cotton. At the time these sight drafts with bills of lading attached were presented to me by the Cotton Company for O. K. I was not informed by the party presenting them and I did not know that the cotton mentioned in the draft or bill of lading attached thereto was cotton covered by trust receipt which the bank was then holding. If I had known that fact I would not have approved the draft as a cash transaction but would have sent the party to the note window to turn in the documents to take up the trust receipts.

#### CROSS EXAMINATION

I don't think I ever sent any representative of the Cotton Company to the note window when they deposited any of these outbound drafts with bills of lading attached. I knew there was quite a volume of business done through our bank by the Cotton Company and I was familiar with the manner in which the bank was handling the Cotton Company's business—that is, I knew that they would buy cotton and that when they wanted to sell the cotton they would come to us and secure the cotton tickets so that they could get the cotton to attach the bills of lading to the drafts and that in order to get these cotton tickets they would have to go to the note department and give a trust receipt therefor. I knew the Cotton Company was selling cotton covered by the trust receipts. That is the purpose for which the cotton tickets were sur-



(Testimony of E. T. Pettigrew.)

rendered by the bank to the Cotton Company. I did not check to determine whether outbound drafts deposited with us covered cotton tickets which were originally attached to four or five different acceptances. I do not know how the Cotton Company did pay the acceptances which were paid at the bank or whether they were paid. I did not handle that. I did not make the arrangement as to how monies should be deposited by the Cotton Company in the bank and I do not know who made that arrangement. I had nothing to do with the opening up of the account between the Cotton Company and the Bank. I was a vice president of the bank at that time. I did not discuss that matter with any other officer of the bank. I know that the Cotton Company was extended a credit of \$200,000.00, as I attended a Directors' meeting when that credit was extended. It is usual and customary for me to approve for a customer such as the Cotton Company any outbound draft so that it might be deposited as a cash item. It is customary to permit any large brokerage concern which is doing a large volume of business where a line of credit has been extended, to deposit outbound drafts as cash items.

"Q Who, representing the Cotton Company, did you ever have a conversation with regarding these deposits?

A I don't think I ever had any conversations with anybody.

Q You know Mr. Norsworthy, do you not?

A Yes sir.



(Testimony of E. T. Pettigrew.)

Q He more frequently than Mr. Sears came with these outbound documents, did he not, for your approval?

A Yes, I think so.

Q Was Sears very often in the Bank?

A I don't think he was. I don't recall him there very often.

Q Did Mr. Norsworthy make any representations to you at the time he got your O. K.?

A Not that I know of.

Q Did Mr. Sears?

A No.

Q You approved them because you considered the Cotton Company was entitled to the credit?

A Yes sir. We had confidence in the company."

I never checked to ascertain whether or not the cotton that was covered by the outbound documents was the same cotton which was covered by the acceptances held in the note department because we had confidence in the Cotton Company. I don't know the manner in which the Cotton Company was paying the acceptances. This system of O.K.'ing outbound documents to be deposited as cash items obtained during the whole period that the Cotton Company did business with the plaintiff bank. Mr. L. O. Ivey was in charge of the note department and it was his duty to ascertain overdue notes or overdue accounts receivable. He was not charged with the duty of reporting to any particular officer of the bank.

(Testimony of E. T. Pettigrew.)

I don't recall that the large indebtedness of the Cotton Company to the bank was ever discussed with me by Mr. Ivey or any other officer of the bank prior to the death of Mr. Sears.

We have no definite rule in the plaintiff bank regarding the time which the bank will carry demand paper. The note department usually reports any paper that is unusually long. At the time I O.K.'d the outbound drafts with bills of lading attached, I made no record of the description of the cotton that was being sold. If I had known that the cotton covered by these outbound drafts was cotton for which the bank held trust receipts, I would not have approved the outbound drafts as a cash collection but would have sent it over to the note window. I didn't know that an arrangement had been made with the bank for depositing these outbound documents covering trust cotton in its checking account and the drawing of checks to the acceptance window. My O.K. or my refusal to give an O.K. would not have depended upon my checking up to see whether that arrangement had been made. The plaintiff bank handled quite a few accounts for brokers, and right along we honored drafts for customers permitting same to be deposited as cash items without any special arrangement being made. The plaintiff bank had no brokerage accounts where the broker was permitted to sell the collateral for which the bank held trust receipts and deposit the proceeds therefrom in his general checking account and then take a check over and take up the collateral and I

(Testimony of E. T. Pettigrew.)

should say that it is not the usual custom to allow brokers to do this. I do not know whether it would have been physically possible for the Cotton Company to have taken the outbound documents and applied them at the note department on any particular acceptance. The detail of such would have been handled by Mr. Ivey.

“Q. Do you know how the Cotton Company paid the bank the acceptances that were paid?

A No, I do not.

Q Did you not testify at the previous trial that it was paid by check?

A I don't know. I don't think so.

MR. PARKE: I refer to page 72 of the witness' testimony, if I may.

Q Let me read your testimony.

MR. COSGROVE: We will stipulate that that is the only way they ever paid anything, by check; and, if you wish, that he knew that was the way it was being paid.

Q BY MR. PARKE: (reading) 'Do you know how the cash was paid to the Bank—what acceptances were paid *paid*? A. No. I think they usually give a check for them. Q A Check drawn on what? A Our Bank. Q Drawn on the same account in which the outgoing drafts were deposited? A Yes.' Do you remember so testifying?

A Perhaps I did. I don't remember. I said 'I think'; I didn't make any positive statement that that was the way it was done.

(Testimony of E. T. Pettigrew.)

Q Now don't you have some knowledge of the fact that the drafts were paid by check?

A No.

Q Now I will continue reading: 'And that was the reason, was it not, Mr. Pettigrew, why you O. K.'d the outbound draft as a cash deposit, in order that the cash might be available at the acceptance window to pay the acceptances? Isn't that correct? A. Yes. I would like to add to that that they could use the money that was deposited in this account for other purposes.' Do you remember so testifying?

A Yes.

Q You knew that they used the moneys of their general checking account for purposes other than the payment of acceptances, did you?

A I knew they could.

Q (Reading) 'You mean in the general operation of their business? A Yes sir. I didn't testify, for instance, when I O. K.'d this draft, that they turn around and make a check to any department with that money.' That is correct, is it not?

A Yes sir.

Q. (Reading) You understood that this money would be deposited in the general checking account of the Cotton Company?

A Yes sir.

Q 'Against which it was privileged to draw checks to pay acceptances in the note department of your Bank or to pay its general operating expenses? A Yes sir.'

A Yes."



(Testimony of John M. Rugg.)

JOHN M. RUGG,

a witness called on behalf of plaintiff, and being duly sworn, testified as follows:

I am one of the vice presidents of the plaintiff bank and knew J. B. Sears.

Thereupon there was exhibited to the witness a draft marked "Plaintiff's Exhibit 8," being a sight draft drawn by the Cotton Company on Stewart Brothers Cotton Company, New Orleans, Louisiana, and his attention was directed to a pencil notation in the upper left hand corner which the witness testified as being his initials J. M. R.

I placed those initials thereon so as to enable the Cotton Company to deposit the outbond draft in their account as a cash transaction. Without such an O. K. of one of the vice presidents or the president, such draft could not go through as a cash transaction. The notations upon the draft refer to the bales of cotton represented by the bill of lading attached thereto. I examined the sight draft before I approved it. I was not informed and I did not know that the cotton covered by the bill of lading attached to the draft which I O. K.'d was also covered by trust receipts held in the Note Department of our Bank as collateral for acceptances of the Cotton Company. If I had known that fact I would not have O. K.'d the sight draft as a cash transaction, but would have referred it to the Note Department.

(Testimony of John M. Rugg.)

### CROSS EXAMINATION

I knew that the Bank had extended to the Cotton Company a \$200,000.00 line of credit, but I have no knowledge whatever of the details of the cotton situation and I simply O. K.'d the drafts with bills of lading attached covering cotton for the credit of the Cotton Company's account and without any particular attention to their loan account. We had absolute confidence in the company, and in Mr. Sears. I did not know with whom, if anybody, the Cotton Company had made arrangements for paying its acceptances by check drawn on the funds realized from the sale of cotton and deposited in the form of these outbound drafts. And I did not know that that was the way it was paying its acceptances, and I made no check of that. Each officer of the Bank has special duties but the vice-presidents all mix into the general loaning. I knew nothing of the general arrangement by which the Cotton Company was handling its business with our bank except that I knew or rather I assumed they were giving trust receipts, but I have no knowledge whatever of the detail operations of the Loan Department. All I knew about the Company's transactions was just their bills of lading with drafts attached and the fact that they had a \$200,000.00 line of credit. Had I known that the acceptances in the Note Department were being paid by checks drawn on the Cotton Company's general checking account, I would not have O.K.'d the drafts as a cash transaction.

(Testimony of John M. Rugg.)

“Q BY MR. COSGROVE: In other words, where the Citizens National Bank holds in its hands a trust receipt given to it in order that an evidence of ownership of a chattel may be taken from the bank, when that evidence of ownership comes back you do never put that through as a cash transaction but make that deal go through the note department, do you not?

A Yes.

Q And that is irrespective of who the man is that is dealing with you?

A Yes.

Q. BY MR. PARKE: Now if it appears from the testimony in this case that the Cotton Company for more than a year had been taking this trust cotton, giving trust receipts, selling the cotton and depositing the proceeds in its general checking account and then drawing a check from time to time which it took over to the acceptance window, who would have made that arrangement to permit that to be done if you say you would not?

MR. COSGROVE: We object to the question on the ground that it assumes as in evidence facts to which there is no testimony. The false hypothesis is that these officials or somebody knew that this matter was being transacted for a year or more, and he is asked, if he would not have made that arrangement who would have made it. Now it is our contention—and the purpose of putting these witnesses on the stand is to show—that nobody knew the manner in which Sears was operating, and that he had covered



(Testimony of John M. Rugg.)

this thing up, and these men never knew and never suspected until his suicide that he was doing business in this way.

MR. PARKE: Do you mean to convey to the Court the idea that they transacted business in this way for a year without the bank knowing that they were selling the trust cotton, depositing in their checking account, and that they were taking checks from the checking account over to the acceptance window and paying particular acceptances? I cannot say that any one particular bank official knew all these steps, because it went through various departments; but it would be ridiculous for counsel to urge to the Court that the bank did not know that trust cotton was being sold, and the proceeds were being deposited in the checking account and the checks were being drawn, because they were receiving the checks—not this man but some other bank official.

BY MR. COSGROVE: Q Starting up in January, where you had these collateral tickets that the loan required as security and it was desired to take those out in order to sell the cotton, and the bills of lading and draft for the sale of that cotton were coming back to the bank with nothing more said about it, where would that go, the draft and the bill of lading?

A If it was presented to us with the bill of lading attached?

Q If that went normally in accordance with business practices of the bank where would it go?

A To the credit of their account.



(Testimony of John M. Rugg.)

Q Now that would be understood, would it, to be the arrangement where a trust receipt was left in lieu of a cotton ticket?

A Yes.

Q Now counsel has asked you if there was a change in that and if, as a matter of fact, instead of returning bills of lading and drafts to the loan department, the Cotton Company had paid by checks against a general checking account over into the loan department to satisfy some of these loan applications covered by these trust receipts, who would have made the change in the arrangement, or who was authorized to do it? That is what he is getting at.

A I think the President of the Bank. The details would be handled by Mr. O. L. Ivey, who I believe would refer it to the President of the bank for approval.

BY MR. PARKE: Q And do you know whether that arrangement was made between Mr. Waters and—

A No sir, I do not.

Whereupon it was stipulated that Mr. Doran, a witness on behalf of plaintiff and vice president of the plaintiff bank, would be deemed to have testified on both Direct and Cross Examination the same as the witness E. T. Pettigrew.

The deposition of

(Testimony of J. P. Conduit.)

J. P. CONDUIT,

a witness on behalf of plaintiff, was offered in evidence, as follows:

I was a director of the Cotton Company and was acquainted with Mr. Sears, Mr. McDevitt, Mr. Hartke and Mr. West.

“Q Did Mr. Sears, at any time between November 1, 1919, and May 1, 1921, inform you that he was selling cotton for which he had given the Citizens National Bank trust receipts and applying money received from the sale of the cotton for purposes other than the satisfaction of acceptances to which the trust receipts were attached?

MR. PARKE: May we have the same objection to that question as to similar questions asked of Mr. McDevitt and Mr. Hartke?

THE COURT: The objection will be overruled.

MR. PARKE: Note an exception.

A He did not.

Q BY MR. COSGROVE: Did you know at any time between the 1st of November, 1920, and the 1st of May, 1921, that Mr. Sears was selling cotton which he had secured from the bank and for which he had given trust receipts and was applying the proceeds from the sale to the satisfaction of indebtedness other than the indebtedness on the acceptances?

MR. PARKE: May we have the same objection?

THE COURT: The same ruling.

MR. PARKE: Note an exception.

(Testimony of J. P. Conduit.)

A I did not.

Q. BY MR. COSGROVE: If you had known in November, 1920, and subsequent thereto and prior to May 1, 1921, that the money which Mr. Sears was using to defray the expenses in conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have objected to his continuing the business of the company?

MR. PARKE: May we have the same objection to the same questions heretofore propounded?

THE COURT: Yes; and the same ruling.

MR. PARKE: Note an exception.

THE COURT: Answer the question.

A I should have objected.

Q BY MR. COSGROVE: If you had known in November, 1920, and thereafter and prior to May 1, 1921, that the money which Mr. Sears was using to defray the expenses of conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have objected to his continuing in the position of Secretary of the California Cotton & Factorage Company?

MR. PARKE: May we have the same objection as to the same questions heretofore asked?

THE COURT: Yes; and the same ruling.

MR. PARKE: Note an exception.

A I should have objected strongly."

(Testimony of C. H. Hartke.)

CROSS EXAMINATION

Beyond attending the directors' meetings I took little activity in the Cotton Company's affairs. I had no financial interest therein. I did not know the arrangement between the Cotton Company and the bank for the handling of business.

C. H. HARTKE,

a witness on behalf of plaintiff, being first duly sworn, testified as follows:

I am an attorney. I acted as attorney in the incorporation of the California Cotton and Factorage Company.

"Q BY MR. COSGROVE: Did Mr. J. B. Sears at any time between November 1, 1919, and May 1, 1921, inform you that he was selling cotton for which he had given the Citizens National Bank trust receipts, and that he was applying the money received from the sale of the cotton to purposes other than the satisfaction of acceptances to which the trust receipts were attached?

MR. PARKE: We desire to make the same objection to this question that was made to the similar question asked the President of the corporation, upon the ground it is immaterial whether or not Sears communicated the details of the management of the business, or of the acts performed by him as Manager of the business, in discharging or disbursing the funds of the corporation, inasmuch as it affirmatively appears by the pleadings that Sears was authorized or dele-



(Testimony of C. H. Hartke.)

gated with the duties and powers of managing the business and of drawing funds, and in generally conducting the business as the executive head, and was not charged with the duty of communicating any particular act to any officer of the Cotton Company; for the further reason that it appears by the pleadings and testimony in evidence, introduced by the plaintiff, that all of the acts, particularly the acts now spoken of, were performed by Sears in the discharge of his duties as manager of the business of the corporation, and under the laws that would constitute legal knowledge on behalf of the corporation, irrespective of the manner the particular acts were communicated or known personally to each or any of the corporate officers.

THE COURT: I will overrule the objection.

MR. PARKE: Note an exception.

A He did not.

Q BY MR. COSGROVE: Did you know at any time between the first of November, 1920, and the 1st of May, 1921, that Mr. Sears was selling cotton which he had secured from the bank and for which he had given trust receipts, and was applying the proceeds from the sale to the satisfaction of indebtedness other than indebtedness upon the acceptances?

MR. PARKE: May we have the same objection that has been heretofore stated, upon the ground and for those reasons, that it is incompetent, irrelevant, and immaterial?

THE COURT: Objection overruled.

MR. PARKE: An exception, please.

(Testimony of C. H. Hartke.)

A I did not.

Q. BY MR. COSGROVE: If you had known in November, 1921, and following that time, that the money which Mr. Sears was using to defray the expenses of conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have objected to his continuing the business of the Company?

MR. PARKE: May we have the objection that it is incompetent, irrelevant, and immaterial, on the same grounds.

THE COURT: The same ruling.

MR. PARKE: Note an exception.

A I would not.

Q BY MR. COSGROVE: If you had known in November, 1920, and thereafter, that the money Mr. Sears was using to defray the expenses in conducting the business of the California Cotton & Factorage Company was obtained from the sale of cotton for which the Citizens National Bank held trust receipts, would you have objected to his continuing in the position as Secretary of the California Cotton & Factorage Company?

MR. PARKE: May we have the same objection for the same reasons as stated?

THE COURT: Did Mr. Hartke hold some other office except Secretary?

MR. COSGROVE: Mr. Hartke was a director.

THE COURT: I will overrule the objection.

(Testimony of C. H. Hartke.)

MR. PARKE: Note an exception.

A I would have."

I was a director of the Cotton Company.

#### CROSS EXAMINATION

I took no active part in the affairs of the Cotton Company, except to attend directors' meetings. I owned one share of stock in the Company, but did not pay cash for it. I won't say definitely whether the one share was issued to me for my services or not. I never rendered a formal statement for services upon which was credited \$100.00 for the one share of stock. I would not say as a fact that Mr. West paid for that one share of stock; I don't know what the minds of the executive officers were at the time I was given this share, whether it was considered for legal services or not. I am not certain as to that. Irrespective of who paid for the certificate, it was issued to me for the purpose that I might qualify as a director. I would not say that the share was given to me without consideration. I did all of the legal services of the company and the company would be indebted to me for them. If I had resigned as director I do not know whether I would have surrendered the one share of stock or not. I took no part in the affairs of the Cotton Company other than attending directors' meetings. I never talked over the administration of the Company's affairs with Mr. Sears, and I do not know what arrangement was made between the Cotton Company and the bank as to the line of credit and the manner in which the money should be borrowed and secured,



(Testimony of C. H. Hartke.)

(Trans. on former trial, p. 200 l. 1-3) but I did at the time know about it, having heard it discussed at directors' meetings.

Thereupon plaintiff offered in evidence as plaintiff's exhibit 16, a certified copy of the resolution of the board of directors of the California Cotton and Factorage Company, authorizing the assignment to the plaintiff bank of any rights of the Cotton Company under the bond forming the issues in this case, and also there was offered in evidence as plaintiff's exhibit 17, the assignment by the California Cotton and Factorage Company of the rights and benefits accruing under the bond to the plaintiff herein.

It is stipulated for purposes of this bill of exceptions that the assignment of the rights and benefits of the California Cotton and Factorage Company accruing under the bond to the plaintiff, sued upon herein by the California Cotton and Factorage Company, was in due and legal form and pursuant to resolution of the board of directors of the California Cotton and Factorage Company at a meeting regularly called therefor. The defendant, however, objected to the introduction of the "assignment" Plaintiff's exhibit 17, upon the ground that it is incompetent, irrelevant and immaterial, for the reason that the cause of action, if any existing, under the bond in favor of the California Cotton and Factorage Company is not such a cause of action as is subject to an assignment. The objection so made was overruled by the court and exception taken to such ruling by the defendant.



(Testimony of L. O. Ivey.)

L. O. IVEY,

a witness for plaintiff, was re-called for cross examination.

I believe I read the letter of September 8, 1919, plaintiff's exhibit 5, having seen it about the date it was written. I was familiar in a general way with arrangement made between the Cotton Company and the bank as to the handling of the Cotton Company's business. My duties as manager in charge of the note department gave me general supervision thereof. In this department was handled notes receivable and bills receivable, and there were several tellers therein. It does not, however, regularly handle "outbound documents", that is, drafts drawn on outside parties, unless goods covered by the bill of lading attached to the draft belong to the note department. The bank maintains a regular collection department for the purpose of handling outbound drafts, and a draft with bill of lading attached drawn on a third party outside the city would be handled through the collection department, so that in this case if the Cotton Company deposited a draft with bill of lading attached and did not get the O. K. of a vice president and it did not cover cotton belonging to the note department it would have gone to the collection department. I cannot say that I knew that the Cotton Company was selling cotton evidenced by the cotton tickets surrendered and for which trust receipts were given. I made no inquiry as to what they were doing with the cotton. (Trans. p. 294, l. 20-26—p. 295, l. 7.)

(Testimony of L. O. Ivey.)

I knew that the Cotton Company was in the business of buying and selling cotton, and I gave the cotton tickets to the Cotton Company and accepted trust receipts therefor, pursuant to the plan outlined by Mr. Sears in his letter to Mr. Waters, and pursuant to the instructions of Mr. Waters, the president of the bank. Mr. Waters told me that the Cotton Company was to take out the items on trust receipts and for me to receive therefor outbound documents that came in accordance with the terms of the trust receipts, (Trans. p. 296, l. 1-2.) and while he did not tell me, I naturally assumed that it was to enable the Cotton Company to facilitate the handling of the cotton and the sale thereof. I did know that they were selling the cotton covered by the trust receipts. During the first year of the Cotton Company's business the bank might have handled as much as \$300,000.00 in acceptances for the Cotton Company, and cotton tickets were attached to every acceptance that came to the bank. All of the cotton tickets attached to the 87 drafts which were unpaid at the time of Mr. Sears' death were turned over to the Cotton Company and trust receipts taken therefor. Mr. Sears signed all of the trust receipts. As I have previously stated, the draft would come into the collection department and Mr. Sears would call at the office and accept the draft and we would accept his trust receipt simultaneously, and then they would come over to the trust department. When they were accepted in the bank the acceptance was signed in the collection department. I never person-

(Testimony of L. O. Ivey.)

ally detached any tickets from the acceptances and substituted a trust receipt. So far as I know, Mr. Norsworthy did not surrender any of the trust receipts. Mr. Sears got the tickets. He had to call at the bank and sign the trust receipt, or a representative of the bank called at his office and he accepted it, and the trust receipt was signed and the tickets delivered to him. I never went to the Cotton Company with these acceptances or drafts personally. According to the instructions of our bank, they were delivered to Sears. A great many of the tickets were physically delivered to Mr. Sears right in the bank. No drafts came to the bank with trust receipts attached to them at the time they arrived, the tickets having been detached before they came. I am absolutely sure of that. All these transactions were handled under my personal supervision. I saw every draft when it came in and I passed on it. I am certain that the tickets were not surrendered before the draft came to my bank. The trust receipts are on a form gotten up by the Cotton Company it had them printed.

The Cotton Company did not at any time ever deliver to the note department in the bank a draft with a bill of lading attached covering any of the cotton covered by trust receipts which the bank held. I do not know where the Cotton Company deposited the out-bound documents covering the cotton covered by the trust receipts. I never went into that phase of the Cotton Company's business, and I do not know where they were depositing their money from the sales of



(Testimony of L. O. Ivey.)

cotton. I did, however, receive checks of the Cotton Company from time to time at the note department in payment of the acceptances of the Cotton Company which the bank held, and these checks were drawn on our own bank on the general checking account of the Cotton Company.

“Q And that manner of payment of the acceptances continued from the time the Cotton Company began to do business, did it not, right up until the very last acceptance was paid?

A I believe the California Cotton & Factorage Company would present a check there at the window to the teller and tell him what draft he wanted to take up, and the item was paid by his check, and the trust receipt surrendered, and no further question asked.

Q Well, have you any doubt about that being the situation?

A I think that is the way it was handled in most cases.

Q Now I show you here a large number of drafts that were presented to the Court before, covering the period not only for the first fiscal year but also covering a great many of the drafts that were paid during the second fiscal year.

A Yes, it looks like they all have been marked paid by our note department.

MR. COSGROVE: It is stipulated they were all—

MR. PARKE: And will you stipulate they were all paid by checks drawn on the checking account?



(Testimony of L. O. Ivey.)

MR. COSGROVE: No; I will stipulate that all those checks were paid, and they appear to have been drawn as they recite.

THE WITNESS: These are the paid acceptances, Mr. Cosgrove.

MR. PARKE: Yes; running over both years. Is it stipulated that those were all paid in checks drawn on the checking account?

Q. BY MR. COSGROVE: Is there anything on those to indicate how they were paid, or in what manner they were paid, or when they were paid, or anything about it?

A No.

Q Nothing on them to indicate that?

A No.

MR. PARKE: Does the witness mean there is nothing to indicate when they were paid? Is there a date stamped?

MR. COSGROVE: No, not when, but how.

MR. PARKE: You asked him when.

THE WITNESS: That item shows it was paid by our note department on a certain date, February 9, 1921. Now as to how that was paid, whether by draft on San Francisco, by the California Cotton & Factorage Company's check, or an outbound document, I can't say; but it was paid, and, as I have stated, in most instances, as I remember, they were paid by checks drawn by the California Cotton & Factorage Company on the Citizens National Bank.

MR. PARKE: I can get the bookkeeper—

(Testimony of L. O. Ivey.)

MR. COSGROVE: I think that covers it; does it not?

MR. PARKE: Well, we have checked carefully, and every acceptance that was paid at the note department was paid by checks drawn on the general checking account by the California Cotton & Factorage Company.

MR. COSGROVE: I would like to have you make that proof; I don't know whether it is a fact or not.

Q BY MR. PARKE: You have no independent recollection, as to each and every particular draft, how they were paid?

A No.

Q But your recollection is that most of them were paid by checks drawn on the checking account?

A Yes."

Thereupon the witness was shown an acceptance dated February 6, 1920, to which was originally attached twenty-five cotton tickets, and also trust receipts for the twenty-five cotton tickets, concerning which the witness testified: I understood that the Cotton Company had to sell the cotton in order to get the "outbound documents" referred to in the trust receipt.

"Q This says 'The purpose being to secure delivery of the shipments and secure outbound documents therefor.' You understood that the outbound documents could be secured only when the Cotton Company sold the cotton?

A That is correct. Have it shipped to their order.

(Testimony of L. O. Ivey.)

Q Well, 'which shall be returned to said Bank in cancellation of this receipt.' What did you understand was to be returned to the Bank in cancellation of this receipt?

A Just what the trust receipt says.

Q Well, what does it say? You read it.

A It says 'Document described below, the purpose being to secure delivery of the shipments and to secure outbound documents therefor which shall be returned to said Bank in cancellation of this receipt.'

Q The outbound documents were to be returned to you?

A Yes.

Q But at no time, Mr. Ivey, from September 1, 1919, up until Mr. Sears' death did they ever return to you any outbound documents, to your note department; is that right?

MR. COSGROVE: I object to the question as having been answered at least twice.

MR. PARKE: Is it stipulated that he answered that yes?

MR. COSGROVE: Yes, twice this afternoon.

MR. PARKE: All right.

Q And during all that period of time all of the acceptances and trust receipts that you held were paid and discharged save and except eighty-seven by checks drawn in your favor on the general checking account?

MR. COSGROVE: I object to that on the ground that he has also answered that at least twice.

MR. PARKE: All right; as long as we have no misunderstanding about it."

(Testimony of L. O. Ivey.)

I did not at any time request Mr. Sears to bring back any "outbound documents". The only request I made was about ten days prior to his death, when I asked him to return the cotton tickets.

"A I would like to have the opportunity of explaining this trust receipt and certificate here, if I can, to make it plain.

Q Go ahead.

A Now this is a demand draft. It has got a trust receipt attached on there. If the California Cotton & Factorage Company comes in at any time and presents us a check in payment of one of these items before it is due and wants to take it up we naturally accept the check without asking further questions. It is settled. It is a demand draft and we really haven't demanded payment of it."

Between the dates of November 19, 1920, and April 25, 1921, there accumulated in the note department of our bank unpaid acceptances in the aggregate amount of \$82,000.00, and we held trust receipts covering all of these acceptances. I did not at any time during the aforementioned period, except about ten days prior to Mr. Sears' death, ever make any demand for the payment of any of these acceptances or request the return of any cotton tickets. There was no arrangement made that I know of for depositing outbound drafts in the checking account. Mr. Sears was treated just like any other customer presenting an item there. I don't know who it was deposited the "outbound drafts" of the Cotton Company. I never at any time checked



(Testimony of L. O. Ivey.)

up with Mr. Sears, or any other officers of the Cotton Company, to ascertain whether or not it had any of the tickets covered by trust receipts held by the bank, for the reason that I had every confidence in the integrity of Mr. Sears, and I didn't think it was necessary. When checks were presented at the note department of the bank for payment on acceptances, the amount so paid was applied on whatever acceptance the Cotton Company desired to take up. Mr. Norsworthy, I think, brought a majority of the checks that were delivered to the note departments in payment of acceptances. As I have previously stated, I do not know whether they sold any cotton that was under our trust receipts.

“Q Didn't Mr. Sears tell you that the reason he needed the tickets was in order that he might have them on hand and take cotton from various acceptances and sell it in different classes?

A The trust receipt or agreement didn't say anything—

Q Just answer the question.

A The trust receipt is the agreement it was taken out under—

Q I am asking you if Mr. Sears didn't tell you that it was necessary in selling the cotton to sell it in grades, and that in making up a sale he might take cotton from four or five different acceptances?

A He never told me that.

Q You knew that.

A Why, naturally—”

(Testimony of L. O. Ivey.)

Q. And you did not know that he was selling any of this cotton that you had trust receipts for?

A. No, sir.

I knew the Cotton Company was engaged in the business of buying and selling cotton, and I knew of no other business that it had. The bank kept no record of the cotton tickets for which trust receipts were accepted so as to enable the bank to identify the particular cotton ticket. All we know is that we are entitled to so many bales of cotton and the value of each ticket would depend upon the grade and weight of the cotton evidenced thereby. I can't specify the cotton tickets that belong to the particular acceptances which are covered by any particular trust receipts. After Sears' death the bank received back 385 tickets. The cotton covered by these tickets has been sold and the \$14,000.00 realized therefrom is now held by the bank in the form of a cashier's check. I do not know how any balance which the Cotton Company had on hand at the time of Mr. Sears' death was applied. The Cotton Company owed the bank a considerable sum in addition to the amount evidenced by the acceptances.

I knew that the Cotton market was dropping. At the time I did talk to Mr. Sears shortly before his death, he said that he had all the cotton tickets that were coming to the bank; had them in his safe. He did not specify how many. The actual detaching of the cotton tickets from the drafts or acceptances and the substituting of trust receipts was done in the collection department, but pursuant to my instructions;

(Testimony of L. O. Ivey.)

then after the draft was accepted by the Cotton Company and paid by the bank it was transferred to the note department and it then came under my personal supervision. We were willing to accept a check of the Cotton Company for the amount of any acceptance in full discharge of both the acceptance and the trust receipt attached thereto.

“Q And you were not interested in whether the Cotton Company actually brought you back the outbound document or the money covering the acceptance, were you?

A If he brought us the money before the outbound document, naturally it was settled as far as we were concerned.

Q Well, it didn't make any difference to you which he brought you?

A Well, either one is money, and money is the consideration for the cancellation of a debt.”

It was thereupon stipulated that the “outbound documents” marked as plaintiff's exhibit 8, representing cotton sold by the Cotton Company and for which acceptances were deposited in the general checking account is typical of all the outbound documents.

“MR. PARKE: Yes. And will you stipulate that outbound documents covering all of the 1,091 tickets represented by these trust receipts were covered by bills of lading deposited as outbound documents?

MR. COSGROVE: I do not know, and have not been able to ascertain; but if you say that is the fact and can—

(Testimony of L. O. Ivey.)

MR. PARKE: Mr. Farrar, our auditor, will testify that he has checked each and every single cotton ticket which is missing and which is covered by these trust receipts and that they were deposited in the checking account in evidence by outbound drafts.

MR. COSGROVE: All right; we will accept that stipulation. That is what we allege in the complaint.

MR. PARKE: And I take it it is stipulated that all outbound drafts were paid by the party on whom they were drawn.

MR. COSGROVE: I have stipulated that at your request during your examination. You mean paid by the drawee?"

MR. PARKE: Yes, so that the bank lost nothing.

MR. COSGROVE: We think they lost all this money; but we will argue that later.

Thereupon the plaintiff rested its case.

Whereupon the defendant presented motion for a nonsuit, as follows:

"MR. PARKE: May I inquire the practice of the Court? I understand the rules differ in different jurisdictions, some Federal Judges holding that on a motion for a nonsuit the matter is submitted without the privilege of presenting a defense.

THE COURT: No.

MR. PARKE: That rule does not obtain. At this time, then, if you Honor please, on behalf of the defendant, Maryland Casualty Company we move for the entry of a nonsuit on the ground that no evidence has been introduced which would sustain any finding of



(Testimony of L. O. Ivey.)

this Court that the California Cotton & Factorage Company sustained any loss, within the meaning of the bond sued upon, by reason of any acts of Sears committed by him within the scope of his duties as secretary, it appearing affirmatively from the testimony introduced by the plaintiff that all moneys received by Sears and which came into his hands in trust from his employer the California Cotton & Factorage Company have been fully accounted for and applied in the use and business of the California Cotton & Factorage Company save and except as to the alleged overdrafts in favor of Sears personally, and as to those items there is no evidence that the withdrawals by Sears, if any, in excess of the salary due him, were made with any fraudulent intent or in violation of any of the provisions of the bond.

We move for nonsuit upon the further ground that no evidence has been introduced by the plaintiff showing the value of the security or securities, to wit, the cotton tickets, which are alleged to have been converted and the proceeds misappropriated or else misapplied by J. B. Sears while in the performance of his duties as secretary of the Cotton Company, the liability in this case, if any, being predicated upon the failure to return the cotton tickets rather than upon the face value of the acceptances.

We move for nonsuit upon the further ground that it appears that the losses, if any were sustained by the California Cotton & Factorage Company by any acts of J. B. Sears, were by reason of acts performed by

(Testimony of T. J. West.)

him in the exercise of his duties as general manager and not as secretary of the Cotton Company and are not covered by the bond sued upon herein.

We move for nonsuit upon the further ground that it affirmatively appears from the testimony introduced in evidence that the California Cotton & Factorage Company failed to comply with the conditions precedent in its application, which conditions were necessary to be fulfilled before it could sue upon the bond, in this, that it failed to have the books, accounts, stocks and securities inspected, audited and approved each month by T. J. West, treasurer of the Cotton Company.

I do not want to argue the motion, because it involves the merits or gist of the action.

THE COURT: Of course I will hear you on the propositions which you have raised in your motion, but I think you had better introduce all your testimony and argue the motion at the conclusion. At this time the motion will be denied."

T. J. WEST,

a witness called on behalf of defendant, testified as follows:

At the time the Cotton Company was incorporated I paid in the total \$50,000.00 capital invested and had issued to me 496 shares of the capital stock.

"Q Do you still have that stock?

MR. COSGROVE: We object to that question, if the Court please, on the ground that it is incompetent,

(Testimony of T. J. West.)

irrelevant and immaterial and has no tendency to prove any of the issues in this case."

We object further to the question as calling for the conclusion of the witness. He should be compelled in this connection to recite the facts.

THE COURT: As to whether he has the stock—the physical possession of it—you may answer; that is, whether he has in his possession the certificates of stock.

"A I haven't got the first certificates that were issued to me."

The first certificates which were issued to me were sent in to the Secretary of the Company for transfer.

Q BY THE COURT: What did you do with the stock when you parted with it?

A Sold it to Sears.

Q BY MR. PARKE: To J. B. Sears?

A Yes.

Q How many Shares?

A 496.

Q And when did you sell the stock to Mr. Sears?

A In the latter part of August, 1922.

Q And what, if anything, did you then do with the original certificates issued to you?

A Sent them in to the secretary to be transferred."

Thereupon the witness was shown a book which it was stipulated is the stock certificate book of the California Cotton and Factorage Company. The witness testified he did not personally see the certificates made out. New certificates were issued to J. B. Sears for

(Testimony of T. J. West.)

496 shares. Whereupon it was stipulated that the original certificates so issued to J. B. Sears were introduced in evidence in a prior trial of this action and later withdrawn and copies substituted, and thereafter and after the conclusion of this trial said original certificates were again filed with the Clerk and made a part of the records of this case. It was further stipulated that for purposes of action of this trial that copies of the said certificates might be used. Thereupon the witness further testified:

The original certificates issued to J. B. Sears are in the office of my attorney, Mr. Ward Chapman.

“Q Now you said it was along about August that you sold out to him?

A In the latter part of August, 1920.”

I attended one directors' meeting of the California Cotton & Factorage Company after the date when I sold my stock to Mr. Sears. That meeting was in the spring of 1921; being the meeting of September 1, 1921. That is the only meeting I attended after I sold my stock in the Company.

Whereupon the minute book of the California Cotton & Factorage Company was introduced in evidence and marked as defendants Exhibit A. It is stipulated that the meeting of September 1, 1921, was called for the purpose of passing resolution authorizing the assignment to the plaintiff of the cause of action sued upon herein.

Prior to that meeting I had a conversation with Mr. Cosgrove, one of the attorneys for the plaintiff.



(Testimony of T. J. West.)

I told him I did not think I could sit legally in the meeting; that I had sold my stock. He said they had not replaced me and that I showed as a director and it would not created any liability, and it would be a courtesy for me to serve, and I did so.

I did not at any time make any check of the written statements which were prepared by Mr. Norsworthy, with the books of the Company. I did receive and examine, however, a statement showing the transactions of the Cotton Company's business for the first year, but I do not now recall its contents.

The application made by the Cotton Company to the defendant herein for the bonds sued upon was signed by me, and that portion which was written in ink is in my handwriting. I don't remember whether I ever saw a trial balance book of the Cotton Company or not. I never made any check of the trial balance book.

#### CROSS EXAMINATION

I signed the certified copy of the resolution of the Board of Directors of the Cotton Company providing for the transfer to the plaintiff bank of the rights under the bond sued upon herein. I was elected Treasurer of the Cotton Company at the first meeting of its board of directors. I never handed in a written resignation as a director or as treasurer. I was a director of the corporation. At the time I sold my stock to Sears about the last of August, 1920, there was one share of stock left in my name. We had no particular arrangement about it; in fact, nothing was said. Sears gave me a note in payment for the stock

(Testimony of T. J. West.)

which I sold to him. The note didn't come along, however, until in December, 1920. The reason I disposed of my stock was because I had more than I could attend to and Mr. Sears and Mr. McDevitt wished to continue the business, and I gave them a chance to work it out. The prospects were bright and they had a good start.

Thereupon there was exhibited to the witness and introduced as plaintiff's Exhibit 18 the promissory note dated December 1, 1920, which said exhibit is in words and figures as follows, to-wit:

PLAINTIFF'S EXHIBIT NO. 18

"\$49,600.00

Los Angeles, Calif., December 1st, 1920.

As hereinafter provided, after date for value received, I promise to pay to the order of J. B. Sears at Los Angeles, California,

FORTY NINE THOUSAND SIX HUNDRED  
DOLLARS

with interest thereon at the rate of 7 per annum from date until paid, payable annually, and ten per cent additional on amount of principal and interest for attorney's fees if placed in the hands of an attorney for collection, or suit, which said \$49,600. is due and payable as follows:

\$10,000.00 on the 1st day of April, 1921,

10,000.00 one year after date, or December 1st, 1921,

10,000.00 two years after date, or December 1st, 1922,

10,000.00 three years after date, or December 1st, 1923,

(Testimony of T. J. West.)

9,600.00 four years after date, or December 1st, 1924

In event said payments or any of them, are not paid at maturity as above specified, then and in such event the owner and holder of this note shall have the privilege of declaring said note due and payable, and it shall then become due and payable.

This note is secured by a pledge of the following securities:

496 Shares of the capital stock of the California Cotton & Factorage Company.

And in the event of the nonpayment of this note or any *instalment* thereof, at maturity, the said J. B. Sears, or owner and holder of said note, is hereby authorized to endorse, transfer, hypothecate, sell or convey said collaterals, or any collaterals substituted for any part thereof, or added to, or any part thereof or cause the same to be done at public or private sale, with or without notice or demand of any sort at such place and on such terms as the said J. B. Sears, or owner and holder of said note, may deem best, and the said J. B. Sears, or owner and holder of said note is authorized to purchase such collaterals when sold for their own protection, and the proceeds of such sale, transfer or hypothecation shall be applied to the payment of this note together with all damages, interest, cost and charges, due or incurred, by reason of its nonpayment when due, or in the execution of this power.

The surplus, if any, after the payment of this note, and any and all other indebtedness due by the under-



(Testimony of T. J. West.)

signed occasioned by the premises to the said J. B. Sears, or owner and holder of this note, together with all costs as above stated, shall be paid to the maker of this note. If the proceeds of such collection or sale shall not be sufficient to pay this note, cost, and all other indebtedness, the maker agrees on demand to make good any deficit.

(Signed) T. W. MCDEVITT.

(U. S. Rev. Stamps \$9.05 cancelled).

(Endorsed on back thereof:) Pay to the order of T. J. West Company, Calexico, Cal.

(Signed) J. B. SEARS."

Thereupon there was exhibited to the witness and introduced in evidence as plaintiff's exhibit 19, the following agreement:

#### MEMORANDUM

This is to certify that, that certain note in the principal sum of \$49,600, dated December 1, 1920, signed by T. W. McDevitt, in favor of J. B. Sears, with interest at the rate of 7% per annum, payable in four installments of \$10,000 each April 1, 1921, December 1, 1921, December 1, 1922 and December 1, 1923, respectively, and \$9,600 on December 1, 1924, has been and is fully paid, satisfied and hereby cancelled, and acknowledged to be of no force and effect, and the said T. W. McDevitt is hereby relieved of all responsibility



(Testimony of T. J. West.)

and liability for the payment of said principal or interest thereon or any part thereof.

It is understood, however, that said note will be forthwith delivered to C. H. Hartke and Ward Chapman, attorneys for the defendants in the case of Macdiarmid etc. vs. McDevitt et al, #112970, now pending in the Superior Court of Los Angeles County, as trustees. Said note shall be marked paid by the payee and held by said trustees to be used as evidence, if necessary, in the aforesaid case, and shall thereafter be delivered to said T. W. McDevitt paid and cancelled and acknowledged to be of no force and effect, as aforesaid.

Said T. W. McDevitt agrees in every way to cooperate with the other defendants in the above-entitled case to properly present and maintain the defense of same, both by way of answer and in the trial thereof.

It is further understood and agreed that the note heretofore executed by the McDevitt Cotton Company in favor of the California Cotton & Factorage Company, under date of April 6, 1920, in the principal sum of \$32,437.29 shall be delivered and transferred to T. J. West Company.

It is also understood that no action at law shall at any time be instituted against T. W. McDevitt, personally or as a stockholder of the McDevitt Cotton

(Testimony of T. J. West.)

Company, for the payment of the principal of the foregoing note or any part thereof.

T. J. WEST COMPANY.

BY T. J. West, Treas.

January 4, 1923.

.....  
.....  
.....  
.....

(The last paragraph and the signature of "T. J. West, Treas." thereto are upon the original of said Exhibit 19 stricken out by ink lines drawn through the same.)

For the 496 shares of stock, Mr. Sears delivered to me the note of T. W. McDevitt for \$49,600 and I received it subsequent to December 1, 1920. I observe that it was endorsed to the order of T. J. West Co. of Calxico. The stock which I sold to him stood in the name of T. J. West. Sears did not tell me what the consideration from him to McDevitt was for this note. I observed the provision in the note that it was secured by a pledge of 496 shares of the stock of the Company, and I knew that McDevitt only had one share. I knew that McDevitt did not have 496 shares of stock in the Company, and I knew that the 496 shares referred to in the note was held by me prior to the sale thereof to Sears. I talked to Sears about the matter and he asked me if I would take his note or McDevitt's note, and I told him it made no

(Testimony of T. J. West.)

difference to me. When I received the note, plaintiff's Exhibit 18, I did not receive the 496 shares of stock. I know I got the 496 shares of stock sent to me before the note. The note came afterwards. The 496 shares of stock were sent to me through the mail and the note came to me later. The 496 shares of stock that was mailed to me was made out in Sears' name, being the stock issued when I surrendered my 496 shares. At the time I received the note I had the 496 shares made out in Sears' name. I understood that the 496 shares of stock I had or received was the 496 shares that was understood to be pledged as provided in the note of December 1, 1921. The 496 shares were in the name of T. J. West until the transfer to J. B. Sears. I understood that the note was secured by the 496 shares of stock that I then had in my possession, and at the time when McDevitt made out the note and delivered it to Sears, and before Sears endorsed it and delivered it to me, the 496 shares mentioned in the note were in my safe and had been there ever since they were transferred. The six certificates for 496 shares that were made out in the name of J. B. Sears some time in the fall or early winter of 1920, were sent down to me pursuant to my arrangement with Sears. When I sold the stock to Sears I required that he surrender that stock made out in his name back to me as security, endorsed in blank, and the stock which he surrendered to me was endorsed in blank. Sears never paid me anything on account of the note.



(Testimony of T. J. West.)

I personally had no business with Shepard & Gluck of New Orleans. I knew who they were, and I knew the Cotton Company had business dealings with them, and I knew at the time I talked with Sears about the transfer of my stock into Sears' name and the endorsement of it by Sears in blank, that Shepard & Gluck had a claim against the Cotton Company in the sum of about \$27,000.00. Hartke was secretary in the Fall of 1920. I recall in the fall of 1920 going to Mr. Hartke, and saying to him, "What is the last date that my name appears as a director of the California Cotton & Factorage Company." He looked it up and told me what date it was. It was prior to May 24, 1921, and it was agreed that the stock certificates should bear the date May 24, the ending of the business year.

Q Now when was it that you talked to Mr. Hartke about this matter of the last time that your name appeared as a director?

A Right after we made the sale.

Q Now was it not along about the first of December?

A No sir.

Q You think it was along in August?

A No sir. That stock was transferred between the 1st and 9th of September, and this note came on to me—

Q I am not asking you anything about that now; I am asking you what was the date of your conversation with Mr. Hartke about the last time your name appeared as a director.



(Testimony of T. J. West.)

A It was between August 25 and September 9.

Q You then instructed Mr. Hartke to have the certificates of stock made out in Sears name, did you not

A Yes sir.

Q And you told him to have them dated back to May 24; is that correct?

A Yes sir.

Q And they did date them back to May 24, did they not?

A Yes sir.

Q But, as you now recollect, that incident took place along between the 25th of August and the 1st of September, 1920?

A Yes sir."

At the time I received the note for \$49,600.00, endorsed by Sears, I did not have any conversation with McDevitt about it. The only conversation I had regarding the note was whether I would take Sears' note or McDevitt's note, or Sears' note endorsed by Mr. McDevitt. We talked that over and I said it didn't make any difference to me, whatever the understanding was between them with regard to the ownership of the stock I do not know. I did have a conversation with McDevitt along about January, 1923, at which time the matter was discussed with Mr. Hartke and Mr. McDevitt. At that time I had gotten into some difficulties.

There was exhibited to the witness the document, plaintiff's Exhibit No. 19, and the witness testified concerning it as follows:

(Testimony of T. J. West.)

The instrument was prepared in Mr. Hartke's office after a conference between myself, Mr. Hartke and Mr. McDevitt. It was signed in the office of Mr. Ward Chapman, my attorney, and he drew the lines through my name the day I signed it. The paper was given to me by Mr. Hartke and my recollection is he walked from his office over to Mr. Chapman's office with me, and I think each of us had a copy of the document.

Q Or two or three copies of it. Didn't you at that time discuss this stock transaction between you and Sears—I mean, by that time, didn't you, in Hartke's office, in the presence of Hartke and McDevitt, on or about January 4, 1923, discuss with those two gentlemen this stock transaction with Sears and the giving of this note by McDevitt to Sears and its endorsement to you?

A No, we didn't discuss that.

Q All right. Now you don't need to say anything more; you have answered that question. If you didn't discuss that how do you account for writing into this memorandum at that time a reference to that instrument?

MR. PARKE: If your Honor please, we object to it upon the ground that it does not appear that this witness prepared this memorandum. It was prepared by Mr. Hartke.

A Hartke did the preparing; I didn't do it.

Q BY MR. COSGROVE: Did you know what was in it?

(Testimony of T. J. West.)

A Yes.

Q You were familiar with its contents, were you not?

A I read it.

Q Well, if you didn't discuss at that time any reference to this \$49,600 note did you make any statement to Mr. Hartke and Mr. McDevitt after reading it respecting the insertion of a reference to that \$49,600 note?

A Well, we talked about the \$49,600 note, but we didn't talk about the sale of the stock.

Mr. McDevitt took the stand that he did not feel liable for that note and was willing to give me a note that he did feel liable for. I talked the matter over with my attorney, Mr. Chapman, and he thought at first we might agree, but then in view of the fact that there was an intention of a suit being filed against me by Shepard & Gluck on stockholders' liability that I should retain that note to show what I sold that stock for. That is what my attorney told me. He also told me that the Shepard & Gluck of New Orleans had threatened suit against me on a stockholders' liability.

Whereupon the document, plaintiff's Exhibit No. 19, was offered in evidence to which objections were made as follows:

"MR. PARKE: We renew our objections, your Honor, it not being a document prepared by this witness, never executed and delivered. The conversations he had or instructions that he gave I think are pertinent, but what somebody wrote out, it seems to me,

(Testimony of T. J. West.)

unless it is officially signed and delivered, would not be binding.

THE COURT: It may be received for whatever it may be worth.

MR. PARKE: Exception."

It was thereupon stipulated that an action was theretofore brought by an assignee of Shepard & Gluck of New Orleans against the stockholders of the California Cotton & Factorage Company, being action No. 112970.

#### RE-DIRECT EXAMINATION.

It was my intention to liquidate and close up the Cotton Company's business at the end of the first year because I was 265 miles away from Los Angeles and had my hands full. Sears begged me not to do so. At that time while Shepard & Gluck had a claim for \$27,000.00 against the Cotton Company, they also had \$17,000.00 of the Cotton Company's money on their accounts, so that the difference between the two business concerns was really nothing. I could have liquidated the affairs of the Cotton Company and had the Pauley note and the McDevitt Cotton Company note and still had forty or fifty cents on the dollar with a hundred bales of cotton. I never received a certificate for one share of stock after I sold my 496 shares to Sears.

Whereupon the stock certificate book of the California Cotton & Factorage Company, showing the cancellations of the certificates of stock originally issued to T. J. West and the issuance of the certificates to J. B. Sears was offered in evidence, to which objections were made as follows:



(Testimony of T. J. West.)

“MR. COSGROVE: We object to the introduction of the instrument on the ground that it discloses cancellations upon its face, alterations upon its face, and that no explanation has been made by the party proffering the document of the alterations.

MR. PARKE: We promise the Court to—Mr. Norsworthy was present when the change in the issuance of these last certificates was made.

THE COURT: Subject to a further showing of the circumstance, it will be admitted.

The matter of giving me either McDevitt's note or Sears' note was discussed by Mr. Sears in the latter part of August, 1920. I told him he could make out the note and send it along to me when he got ready—transfer the stock and send it down. Sears and McDevitt were to transfer the stock and send it down and then settle the agreement between themselves and send me one note or the other. My conversation was not with Mr. McDevitt but with Mr. Sears. Sears said he and McDevitt wanted to continue the cotton business and that he and McDevitt had been talking about it and they were making some agreement between themselves and Sears stated he would either send me his note or McDevitt's note to him endorsed by him to me. I told him it made no difference to me and that they could, when they made their final agreement, send the note along. I then returned to Calexico. At that time the original certificates of stock were in my safe at Calexico and after I reached there I endorsed the certificates in blank and mailed them in either to J. B.

(Testimony of T. J. West.)

Sears or the California Cotton & Factorage Company to be transferred.

“Q And how long after you sent in your certificates endorsed in blank for transfer was it that the new certificates made out in the name of J. B. Sears were sent down to you?

A In the first part of September.

MR. COSGROVE: That is not responsive.

Q BY MR. PARKE: No; how long between the two dates?

A Two weeks.

Q And you have retained the certificates made out in Sears name and which were mailed to you ever since, have you?

A Yes sir.”

I was satisfied to have the note made out T. J. West Company.

Q Now just state to the Court if any conversation was had by you with anybody regarding the date which should be filled in the certificates that were to be issued to Sears?

A Yes, I did.

Q Who did you talk to?

A Well, I had made the sale on the basis of ending the business April 30.

MR. COSGROVE: We move to strike that out as not responsive and a conclusion.

Q BY MR. PARKE: Well, who did you talk to?

A Mr. Sears.

Q State what you said to him?

(Testimony of T. J. West.)

A And I wanted to be relieved of any responsibility for the incoming season's business. I wanted to withdraw from my responsibility. And we agreed then—

Q No, just what was said. Do you mean by "agreed" that it was stated?

A It was stated that we would transfer the stock back then to the end of the business year, and I remarked that 'We can't transfer it farther back than where I appeared in a meeting of the board of directors.' So we then went to Hartke and found that it could be transferred as of May 24. We would have transferred it April 30 if we could, at the end of the business year. And then it was done."

#### RE-CROSS EXAMINATION

During the last of August or first of September when the discussion was had regarding the surrender of my certificates and the issuance of new certificates to Sears nothing was said about who was secretary or who should sign the certificates. I knew that Sears had been secretary of the corporation from its inception, but that he went away for a while and while he was gone Mr. Hartke acted as secretary, but I didn't know that when Sears returned he was again reinstated in the position of secretary. Mr. Hartke was secretary at the time I sold out.

Whereupon the defendant offered in evidence as defendant's Exhibit A all the minutes of the California Cotton & Factorage Company and it was stipulated that the following are the only parts desired to be presented for purposes of this bill of exceptions, to-wit:

(Testimony of T. J. West.)

MINUTES OF SPECIAL MEETING OF BOARD  
OF DIRECTORS.

A special meeting of the Board of Directors of the California Cotton & Factorage Company was held at No. 938 Merchants Natinal Bank Building, Los Angeles, California, on the 9th day of September, 1920, at 2 o'clock P. M., at which meeting the following directors were present:

T. W. McDevitt, president; John P. Conduit, vice president; T. J. West, treasurer, C. H. Hartke, secretary, and J. B. Sears, constituting all the members of the board of directors, and being the subscribers for all of the capital stock of said corporation, each member of said board having first signed a waiver of notice of this special meeting.

T. W. McDevitt, president of said corporation, as such, presided at said special meeting.

The minutes of the previous meeting were read and approved.

C. H. Hartke, the secretary of said company, tendered his resignation as such secretary, with the request that same be accepted immediately. After discussion and consideration of same, upon motion, duly made by John P. Conduit and seconded by T. J. West, the following resolution was adopted:

RESOLVED that the resignation of C. H. Hartke as secretary be, and is hereby, accepted, to take effect this date.

Upon motion, duly made by C. H. Hartke and seconded by T. J. West, the following resolution was un-



(Testimony of T. J. West.)

animously adopted by the affirmative vote of all of the directors of said company:

RESOLVED that J. B. Sears be, and is hereby, appointed as secretary of said corporation, to fill the vacancy caused by the resignation of C. H. Hartke.

John P. Conduit, the vice president of said company, then tendered his resignation as vice president of said company, with the request that same be accepted to take effect immediately. After discussion and consideration of same, and upon motion duly made by T. J. West and seconded by J. B. Sears, the following resolution was unanimously adopted by the affirmative vote of all of the directors of said company:

RESOLVED that C. H. Hartke be, and is hereby, appointed as vice president of said corporation, to fill the vacancy caused by the resignation of J. P. Conduit, and that said C. H. Hartke, in the capacity of said vice president and attorney for said corporation, be paid the sum of \$50.00 per month for his ordinary services.

There being no further business, on motion, duly made and seconded, the meeting was regularly adjourned.

C. H. Hartke

Secretary.

Approved:

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President.

(No meetings of directors or stockholders were held between May 20, 1920 and September 9, 1920.)

(Testimony of T. J. West.)

MINUTES OF SPECIAL MEETING OF BOARD  
OF DIRECTORS.

Pursuant to resolution passed by the stockholders at a special meeting held at 10 o'clock A. M., May 20, 1920, at the office of said corporation, the Board of Directors met in special meeting at the office and principal place of business of said company, at 938 Merchants National Bank Building, Los Angeles, California, each director having heretofore signed a waiver of notice of said meeting. The meeting being called to order by President T. W. McDevitt, Directors John P. Conduit, T. J. West, J. B. Sears and C. H. Hartke answered present, being all of the members of said Board.

The Secretary then presented the waiver of notice heretofore signed by each of the directors. There being no objection, it was ordered to be entered in the minutes. The following is a copy thereof:

WAIVER OF NOTICE OF SPECIAL MEET-  
ING OF DIRECTORS.

We, the undersigned, directors of the California Cotton & Factorage Company, a corporation of the State of California, do hereby certify that we separately and severally waive notice of the time, place and purposes of the special meeting of the Board of Directors to be held in the City of Los Angeles, California, on the 20th day of May, 1920, at 4:00 o'clock P. M. at the office of the Company, 938 Merchants National Bank Building,

(Testimony of T. J. West.)

Los Angeles, California, and we hereby consent that the same be held at the above named time and place and we do further consent to the transaction of any and all business that may come before the meeting.

Dated this the 20th day of May, 1920.

T. W. McDevitt

John P. Conduit

T. J. West

J. B. Sears

C. H. Hartke

The attention of the board was then called by the President to the purposes for which the meeting was held, namely, considering and acting upon the resignation of J. B. Sears as Secretary, and considering and authorizing the application to the Commissioner of Corporations for permission to issue the capital stock of said company.

J. B. Sears, the Secretary of said Company, tendered his resignation as Secretary of said company, with the request that the same be accepted and that he be not deprived of any of the powers heretofore granted him by the by-laws as the executive officer of said corporation. After discussion and consideration of the same, and upon motion, duly made by T. J. West and seconded by John P. Conduit, the following resolution was duly adopted by the unanimous affirmative vote:

Resolved that the resignation of J. B. Sears as Secretary of said corporation be, and is hereby,

(Testimony of T. J. West.)

accepted; that he be retained as the Manager of said corporation, at a salary of \$5000.00 per annum; that he is hereby authorized, and is, to retain all the powers and privileges heretofore granted to him under the by-laws to execute all proper instruments for and on behalf of the company, to sign the name of this company to checks, drafts, bills of exchange, receipts, acceptances and acquittances, and to indorse his name on checks, drafts, bills of exchange, notes, and other evidences of indebtedness which shall be valid and binding upon the corporation without the previous authorization or subsequent ratification of any of the officers thereof.

Upon motion, duly made by John P. Conduit and seconded by T. J. West, the following resolution was unanimously adopted by the affirmative vote of all the directors of said company.

RESOLVED that C. H. Hartke be, and is hereby, appointed as Secretary of said corporation to fill the vacancy caused by the resignation of J. B. Sears.

Said office as Secretary was accepted by C. H. Hartke, who immediately entered upon the duties thereof.

Upon motion, duly made by T. J. West and seconded by John P. Conduit, the following resolution was adopted:

RESOLVED that C. H. Hartke, attorney for the corporation, be and is hereby authorized and



(Testimony of James F. Norsworthy.)

directed to prepare and file with the Commissioner of Corporations an application for this corporation to issue \$450,000.00 of its capital stock, in shares of \$100.00 each, par value to the directors of the corporation, in the following manner:

NAME.	No. SHARES	AMOUNT.
T. W. McDevitt	900	\$90,000.00
John P. Conduit	900	90,000.00
T. J. West	900	90,000.00
J. B. Sears	900	90,000.00
C. H. Hartke	900	90,000.00

There being no further business, on motion, duly made and seconded, the meeting was regularly adjourned.

C. H. Hartke  
Secretary.

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JAMES F. NORSWORTHY,

a witness on behalf of the defendant, being first duly sworn, testified as follows:

My home is in Sulphur, Oklahoma. I entered the employ of the Cotton Company in November, 1919, and continued in its employ until Mr. Sears' death. I was bookkeeper for the Company. Prior to my connection with the Cotton Company I was in the cotton seed oil and cotton ginning business. I have had experience as a cotton broker ever since 1900 in Texas buying and selling cotton. I worked for the Planters Cotton Oil Company in Texas. I had known

(Testimony of James F. Norsworthy.)

Mr. Sears since 1903 while he was in Texas. He was employed by the George H. McFadden Cotton Agency ever since he was a bare footed boy. He was practically raised in that office. I am familiar with the manner in which the McFadden Cotton Company conducted its business. When I came to work for the Cotton Company Mr. Sears instructed me to put in the same system that McFadden has and so we ordered the check stub registers and other books and ledgers. We kept a stock book wherein we entered the cotton when we purchased it and also memorandum of the sales of cotton giving the invoice number, from whom purchased, number of the bale, weight of the bale, class of the bale—that is, it was graded—put into classes. It was a bale book or stock book and it showed our stock on hand. I have examined all the books here in Court and that book is not here. It was kept, however, during the whole period the Company was in operation. I remained in the Cotton Company's office until about the 15th or 17th of May, 1921, on which date the books were all turned over to Mr. Bailey. I showed him all the books, where they were in the safe, and gave him the key. The bale book was in the safe at that time. After that I had nothing to do with the custody of the books. I also had a monthly trial balance book. It was in the office at the time the books were turned over to Mr. Bailey. In the trial balance book were also entered the control accounts of the ledger, debits and credits, each month. These were exactly like the

(Testimony of James F. Norsworthy.)

monthly statements which have been testified to. The trial balance book covered the whole period of time that the Cotton Company was in business, the last trial balance having been entered on March 31, 1921. We also kept a check stub book or check register book in which was entered all checks. We also kept a ledger system and a journal; also a "cotton sales" book and a "cotton bought" book. We also kept a record of the indebtedness of the Cotton Company to the Citizens National Bank. It was kept under the account designated as "Acceptances Citizens National Bank of Los Angeles". In the stock or bale book was entered a record of the trust receipts, the numbers, the acceptance number would be put in. In the stock or bale book was entered "the number of the buyer's invoice; and when we would sell the cotton we would then put the sale number in the same book. We would put the number of the bale of cotton, the ticket number, the weight of the cotton, and the cost of the cotton. Then when the classer would classify his list of cotton he would put in his book his class. When we would sell the cotton, under the head 'Remarks' we would put to whom sold, and the date, and the acceptance covering this list would have to bear that number."

Whereupon there was exhibited to the witness acceptance No. 77 for \$2,675.25 and his attention was called to a note thereon which refers to "25 C. R." He testified regarding same as follows:



(Testimony of James F. Norsworthy.)

The acceptance covered 25 Cotton Receipts—that is, 25 bales of cotton. When the cotton arrived at Los Angeles or when the cotton receipts arrive, and they were received from the plaintiff bank, I would enter that information in the stock book from the invoice.

“A The invoice covering this particular 25 bales of cotton would come into our office probably two days ahead of this draft. We would enter it then in our stock book. Then when this draft would come in with the tickets attached we would accept the draft and take over the tickets—that is when it was brought up there by the Citizens National Bank—we would take the tickets off and give them a trust receipt and keep the tickets in our office.

Q And would you then make any record in this stock book of the number of acceptances held by the bank covering those 25 bales?

A Yes sir. It would then bear the buyer's invoice number that had already been entered in the stock book.

Q And those buyer's invoices, who were they mailed to you by?

A By our buyers in the interior, Mr. Snell, Mr. Smith, and Mr. E. E. Snell, buyers in the field.

Q And when you sold any part of that 25 bales of cotton what, if any, entries were made in this stock book?

A They were marked out of the stock book as sold, and the date sold.

Q And was any record entered as to the—



(Testimony of James F. Norsworthy.)

MR. COSGROVE: Now we object to leading the witness.

Q BY MR. PARKE: All right. Go ahead. Any other information?

A Well, we would mark it off, and then we would go and mark the acceptance off—that is the acceptance that we had paid.

Q And were you able at any time *form* the information contained in this stock book to ascertain the number of bales of cotton on hand?

A Yes sir.

Q And were you able from the information reflected in this stock book to show what particular cotton you had on hand by bale numbers?

A Yes sir."

Q. And were you able to ascertain from this book which particular acceptance covered the particular bales of cotton on hand?

A Yes sir."

Mr. Sears would write checks during my absence from the office but the only time I knew of him making entries in the ledger was when I was sick at the close of January, 1920, and he made the closing entries in the ledger carrying them from the journal. I also made two trips to Texas on my own business and I was also sick several times while I was working for the Cotton Company and during my absence Mr. Sears did make entries but it was not his practice to do so when I was in the office.

I was familiar with the manner in which the drafts drawn on the Cotton Company for cotton purchased

(Testimony of James F. Norsworthy.)

were handled by the Citizens National Bank. I was the one who usually took off the tickets from the acceptances and attached the trust receipts. Mr. Sears did that not very often, only when I was out of the office. I frequently went to the plaintiff bank in connection with the Company's business; in fact, almost every day, but Mr. Sears did not go to the bank very often. Most of the cotton tickets were detached at the Cotton Company's office, the drafts and the cotton tickets having been sent by the bank to the Cotton Company's office, probably I have at some time or other gone to the plaintiff bank and made the substitution there, but I don't remember having done so. Mr. Sears attended to the sale of cotton, but myself and Mr. Collins attended to making up what is designated as the "outbound documents".

"Q Now will you state to the Court just your line of procedure when you sold cotton—how you made up the outbound documents and what you did with them?

A Well, we would make a sale of cotton, a list of cotton which would be anywhere from fifty to one hundred or two hundred bales of cotton. We would first get the confirmation of the sale. We would then go to the class book and pick out the sales of cotton—we would sell a certain grade of cotton—middling or strict middling or low. We would go to the class book then and pick out the cotton that would agree with this sale. Probably it would come from different yards—Blythe, Yuma, Bakersfield or Calexico. We would pick out those and send the tickets in to the respective

(Testimony of James F. Norsworthy.)

yards and have the cotton shipped. They would take the cotton to the depot and get a bill of lading and send us the bill of lading. We would attach the bill of lading to the drafts then, make up our account sales, or invoice, deposit the drafts in the Citizens National Bank and take credit for them in our pass book.

Q And would there be anything attached to the draft?

A A bill of lading.

Q What would you do with your account sales after that?

A We would mail those to the purchasers of the cotton, together with weight sheets showing the numbers and weights of the bales.

Q And what, if any, record would you make in your stock book of the cotton that was sold?

A Mr. Collins would then take this stock sheet and go through and mark the cotton off. For instance, if there was a shipment to Gluck or Witherspoon or whoever it might be in the markets, he would put "Witherspoon" inside and the date the cotton was delivered.

Q And was any record kept of the number of bales of cotton sold?

A Yes.

Q Where was that kept?

A In the cotton sales book; the bales and the pounds.

Q And was there any record kept of the physical number of the bale?

A Yes.

(Testimony of James F. Norsworthy.)

Q Where was that entry made?

A It was marked off in that stock book.

Q And was an entry made in any other book?

A No. Just checked off in that stock book showing that the bale had been disposed of.

Q Was it your practice to sell, as a lot, the particular lot of cotton covered by any one acceptance?

A No.

Q Was the cotton covered by any particular acceptance all of the same grade?

A No sir.

Q Who usually took the drafts with the bills of lading to the bank for deposit?

A I did.

Q And what did you do when you got there with the drafts?

A I would go to the Vice President—most of the time I went to Mr. Rugg. I was better acquainted with Mr. Rugg than any of the other vice presidents, and if he was not busy I would always go to him and have him O. K. them and take them over to the receiving teller and deposit them.

Q And get an entry in your pass book?

A Yes sir.

Q Did you ever have any conversation with Mr. Rugg or any of the other vice presidents regarding their O. K. on these drafts?

A No; I would just present them and they would O. K. them. Oh, they would ask me what it was for, probably, and I would tell them a hundred bales or fifty bales of cotton; something like that."



(Testimony of James F. Norsworthy.)

I couldn't say how often Mr. Sears took up the out-bound documents for deposit, but I don't think he went very many times. I attended to the payment of the acceptances held by the bank.

"Q BY MR. PARKE: Well, state what you did in that regard, regarding the payment of acceptances.

A Well, when we would make a deposit covering the cotton I would go to the note department, and there was a young man there, I don't recall his name just now, and I would make him a list giving the number of our acceptance and the amount that I wanted to pay. Probably I would leave the list with him. He would get out the list and I would bring him a check. Sometimes I would leave the list and the check covering so many acceptances—it might be four or five; then I would get the acceptances, and he would then figure the interest, probably that day or next day. He has waited sometimes one or two days and would phone me the amount of interest. I would then issue him a check covering interest on those acceptances I had taken up and either bring it to him or mail it to him."

We paid off the acceptances just as fast as we could sell the cotton. We did not make payment of the acceptances at the note department each day when we made a deposit, the reason that I was probably busy at something else, but if it was not the same day it would be only the next day or two. I determined the amount which we would pay the bank on the acceptances from our records and if we owed \$10,000.00,

(Testimony of James F. Norsworthy.)

and had \$10,000.00 on hand we would apply it. As fast as money was available we paid it on acceptances.

“Q And in taking up the acceptances were the proceeds from any particular cotton applied upon any particular acceptance?

A No sir.

Q Why was that not done?

A We paid no attention to the acceptances; we just took the oldest ones first in order to stop the interest.

Q Would it have been practicable from a book-keeping standpoint to have kept a separate record of the sale of each bale of cotton so that the proceeds from that sale might be applied on the particular acceptance covering its purchase?

A No sir.

Q Why not?

A It wouldn't be any more practicable than it would for a merchant to keep a separate record of each pair of shoes that he buys. He buys the goods and puts them in the merchandise account; we bought cotton and put it in the cotton account. Just one general account of cotton.

Q Did you keep a separate account of the moneys realized from the sale of cotton covered by trust receipts and moneys realized from the sale of other cotton that you purchased?

A No sir. We had the cotton bought and cotton sold accounts.

Q And could you from this cotton bought and cotton sold account at any time determine the amount of cotton on hand?

(Testimony of James F. Norsworthy.)

A Yes sir. The bales bought and the bales sold, and the difference was on hand.

Q And was it possible from your records to identify that cotton by the bale number?

A Yes sir."

I have been keeping books all my life. I was raised in a bank, having worked there about fifteen years and I have been in the cotton business since 1900 and was auditor for a cotton firm for fifteen years, which firm was engaged in buying and selling cotton. In my opinion, as a bookkeeper or auditor, it was not necessary in order to properly reflect the condition of the Cotton Company's business that another account be kept such as Mr. Bailey has designated as "Trust Cotton Account."

"Q Why was it not necessary?

A It would have been impracticable. He would have to make— It would take you all day to make the general entries on account of the fluctuations of the market, unless you set a certain hour in the day. The market fluctuates all through the day. Mr. Bailey's idea is, every time the market changes, I suppose, to make an entry debiting and crediting the cotton.

Q As I understand it, then, if the trust account attempted to carry the market value of the cotton you would have to adjust the entries?

A You would have to adjust the entries every time the market fluctuated.

Q Could you, with the entries which were made in the books, at any time, from an examination of the

(Testimony of James F. Norsworthy.)

entries themselves, tell how many bales of cotton you had on hand which were covered by trust receipts?

A Yes sir. The stock book will show that.

Q And could you from the entries which were made in the books ascertain to which acceptance that cotton applies?

A By checking back, yes sir.

Q And could you from the entries which were made in the stock book and elsewhere determine what had become of those bales of cotton covered by trust receipts which were sold?

A Yes sir."

"Q BY MR. PARKE: How could you do that?

A By the stock book.

Q Well, will you detail for the Court again so that there will be no misunderstanding, just how you could check that up?

A For instance, Mr. Caruse would draw on us from Blythe for twenty-five bales of cotton. He would have twenty-five tickets attached to this draft. We would accept this draft. We would get an invoice from him showing the bale numbers and all, and the weights, and the amount of money, and the exchange, if he had paid any. We would enter that in the stock book, and the buyer's report number. We then knew that this draft— This draft Mr. Caruse drew on us was an acceptance and covered this special invoice under buyer's report No. so and so.

Q And was there any reference made to the number of the acceptance in that stock book?

A I think the buyer's reports will show that.



(Testimony of James F. Norsworthy.)

Q I mean now in the stock book. Did you enter the number of the acceptance?

A We gave the number and buyer's report number and the date.

Q And in all cases where there were acceptances at the bank were there trust receipts given?

A Yes.

Q By connecting up the cotton with the acceptance you were able to tell what was covered by the trust receipt attached there to the acceptance?

MR. COSGROVE: I object to the question.

THE COURT: It is leading, but I suppose it is a recapitulation of what was understood to be his testimony.

THE REPORTER: I didn't get the answer.

MR. PARKE: His answer was yes."

I prepared trial balances of the Cotton Company's business at least once each month, making three copies. I sent one to Mr. West and one to Mr. Neal, Waco, and I kept one on file in the office. I looked through the documents of the Cotton Company, but I do not find any of these statements in the file and I do not find the trial balance book in which they were kept. The last statement which I prepared on March 31, 1921, reflected the true balance,—that is, the financial condition of the Cotton Company. It contained a statement of the amount owing to the plaintiff bank and the amount of cotton on hand. These statements were prepared in the form usually known as trial balance for the period of a month. Mr. McDevitt

(Testimony of James F. Norsworthy.)

was in the Cotton Company's office almost every day for at least a year prior to the time the Cotton Company closed its office. He was frequently in Mr. Sears' office. We all had offices together just one door away and Mr. McDevitt was in Mr. Sears' room probably several times every day. The stock book or class book was kept by Mr. Collins and I used it in making up my monthly trial balances. I got from it the cotton on hand. I prepared a statement showing the condition of the Cotton Company at the end of its first fiscal year, making four copies thereof. One was sent to Mr. Neal and I think one to Mr. West and we kept one in the office but I have been unable to find it among the Company's papers at this time. The monthly statements prepared by me during the first year reflected that the Cotton Company was making profit in its operation while the statements which were prepared during the second fiscal year showed a loss. I can, with the books which are here in Court, demonstrate as to whether there was a profit or loss during either of the years the Cotton Company operated, but it would take considerable time. The statements which I prepared each month did reflect the true financial condition of the Cotton Company.

The reason no entry was made in the books of the Cotton Company regarding the \$75,000.00 loan was because it had nothing to do with the California Cotton & Factorage Company's business. It was a separate department. I talked to Mr. Sears in re-

(Testimony of James F. Norsworthy.)

lation to making entries in the books regarding this loan. When Mr. Sears made the deposit of \$26,000.00 that had been sent him by Mr. West he brought the deposit slip to me and told me to lock it up in the box. I told him it should be entered on the books. He said, "No, it doesn't enter into our books. Mr. Neal doesn't want it in our books at all". At the time they were making the loans I told Mr. Sears that every time the Cotton Company endorsed a note it became liable for it and this contingent liability should be set up on the books, but Sears said he did not want them in the books because, as he said, Mr. Neal had instructed him to keep it out of the books. There was a little auxiliary book, however, in which records were kept by the Cotton Company of its loan account and in which I kept track of the cotton tickets that were held by the bank in connection with these loans.

The witness' attention was directed to an account known as "Suspense Account of J. B. Sears" appearing in the books of the Cotton Company. Concerning said account the witness testified as follows:

Mr. Sears' salary was to be \$5,000.00 a year and 25% commission on profits earned; so he had an overdraft and he needed some money. He bought some furniture, I think in the sum of \$800.00, and he gave a check for that and told me to charge it to "J. B. Sears Suspense". We carried several checks into the Suspense Account, and I think it ran up to about \$1800.00, and we were to hold that until the end of the season when we closed the Cotton Company's books and we were to credit his account with his



(Testimony of James F. Norsworthy.)

25% and clear the suspense account. All of the items in the suspense account were entered during the first year, but no entry crediting commissions was made at the end of the first year because all the Cotton Company's profits were tied up in notes. I talked to Mr. Sears regarding the entry of commissions at the end of the year and he said he could not take his commission until he collected the balance of the notes—that is, the notes of McDevitt Cotton Company and the Pauley notes.

The Cotton Company did not very often hedge its purchases. Sometimes it made a little hedge. There is a hedging account set up in the ledger and such account reflects three transactions that were hedged. Insofar as I know that is all the cases where there was a hedge. I talked with Mr. Sears regarding hedging of purchases at the beginning of the second fiscal year and many times thereafter. He said he wanted to hedge the cotton but Mr. Neal objected to it. The Cotton Company received telegrams from Mr. Neal some times two or three times a week giving advice regarding the cotton market. These telegrams were signed "Viaduct", that being Mr. Neal's code name.

Thereupon it was stipulated that the testimony of the witness concerning the relationship of Mr. Sears and Mr. Neal would be as follows:

"MR. PARKE: It would be to this effect: that throughout practically the whole period of the Company's business Mr. Sears from time to time stated to Mr. Norsworthy that he considered the conduct of



(Testimony of James F. Norsworthy.)

the business to be under the direction of Mr. Neill, and that it was Mr. Neill's money that was invested, and that Neill had been like a father to him and he was sorry that the market was such that he seemed to be up against a stone wall during the second year, and that he hoped from day to day that he would be able to recoup the operating losses that had been made, for Mr. Neill's sake; and further, that Mr. Neill was here only a day or two prior to Mr. Sears' death and that Sears came in after talking to Mr. Neill, to Mr. Norsworthy, crying, and saying that Neill had 'given him hell' for losing money, and that it looked like he was up against a stone wall, and that he simply couldn't stand it and that he hoped every day the market would break and take an upward rise. Now, that is it in substance.

MR. COSGROVE: We will stipulate the witness would so testify."

There are a lot of Cotton companies that hedge and there are a lot of cotton companies that do not hedge according to the condition of the market. I have handled cotton this year and I have not hedged a bale because the fluctuations in the market hedged it for me. By hedging I mean that when we sell a hundred bales of cotton we go on the board and buy a hundred to protect ourselves and by so doing you protect yourself. It costs money to hedge as there is a commission which has to be paid. And it is possible that you will lose your commission on the sale by hedging. I have been buying cotton since 1900 and it is not my practice to hedge.

(Testimony of James F. Norsworthy.)

### CROSS EXAMINATION

I never worked for or with Mr. Sears prior to the time I came with the cotton company. I came to Los Angeles in August, 1919, and went to work for the Cotton Company in November of that year. I was engaged by Mr. Sears. Mr. Sears told me the character of books which I should keep for the Cotton Company and when I was in doubt as to proper entry to be made of any item, I received my instructions from Mr. Sears. Mr. Sears told me not to enter the item of \$26,000.00 concerning which I spoke to him for the reason that Mr. Neill did not want it entered in the books. There was one other matter that I spoke to Mr. Sears about and he told me he did not want it put into the books.

Sometimes Mr. Sears was present when I detached the cotton tickets from the acceptances and attached the trust receipts. The name "J. B. Sears" on the draft was written on there by Mr. Sears at about the same time as we occupied adjoining rooms. I would issue a trust receipt detached tickets and put on the rubber stamp on the acceptance and he would sign the acceptance and the trust receipt. It was all handled as one transaction. The trust receipts were signed by Mr. Sears in his own handwriting. That was also a part of the same transaction and it all occurred at one and the same time, the trust receipts being signed by Mr. Sears at the same time that he signed the acceptances. When the Cotton Company issued a trust receipt a record of it was made in the acceptance book—that is, the acceptance was entered therein and

(Testimony of James F. Norsworthy.)

the trust receipt is attached to it. There is no direct reference in any of the books to a trust receipt. There is no column headed "Trust Receipts Outstanding" in the books of the Cotton Company. The facts are there never would be any such entry if I was keeping the books and no other bookkeeper that I ever heard of would make such an entry. The stock book which I have testified about contained the following information:

"We would receive from our buyers in the interior an invoice covering so many bales of cotton, with that cotton purchase number, and date of invoice. We would enter it in this book, giving the number of bales, the weight of the bales, who received from; then the classer would take this and make a classification sheet; he would come back to this book and from his class sheet he would put in this book opposite the bale number and bale weight the class of the cotton; when we would ship the cotton we would put the date shipped and to whom shipped; a memorandum of draft covering it was one of the entries appearing in the book as well as the entry of the buyer's report and the date of the report."

Mr. Collins and I made up the outbound documents. It was the custom of J. B. Sears to sign all the drafts that went out. I then prepared invoices and Mr. Collins got up the number of bales of cotton that were being sold and then it was presented to Sears and he would sign the sight draft so that it could be deposited in the bank. I did not ever talk



(Testimony of James F. Norsworthy.)

to Mr. Rugg, Vice president of the plaintiff bank, concerning the purpose of his O. K. on the outbound documents. I attended to the payment of acceptances. They were always paid by check. Mr. Sears signed most of the checks but if he was out of town then I signed them. When an acceptance was paid it was checked off on the acceptance account as paid. The last acceptance that was paid to the bank bears the serial number 76 and was paid on March 25, 1921. On that same date three other acceptances were paid. The previous date of payment was January 17, 1921 on which four acceptances were paid and the next previous date of payment was on December 16, 1920, when seventeen acceptances were paid. Likewise on previous dates when payment of acceptances was made several acceptances were paid at the same time.

Myself and C. H. Hartke prepared the income tax report for the Cotton Company. It did not show a profit for the purpose of paying an income tax.

#### RE-DIRECT EXAMINATION

In making up the income tax of the Cotton Company for the first year we charged off as bad debts the loan to the McDevitt Cotton Company and other loans—in fact, wrote off about \$63,000.00. Aside from the bad loans written off, our income tax report would have shown a profit.

There was no change in the manner of keeping the books of the Cotton Company or of handling the acceptances between the Cotton Company and the bank, or in the manner of selling and in depositing outbound



(Testimony of James F. Norsworthy.)

drafts or in the manner of paying off the acceptances at the bank during any of the time that I was bookkeeper. I am familiar with the system of book-keeping kept by McFadden Cotton & Brokerage Company and the system of books which I kept for the Cotton Company was, as Mr. Sears told me, the same system that it kept.

The loans that were made by the Cotton Company to the McDevitt Cotton Company arose in this way; the man working for McDevitt would draw on the McDevitt Cotton Company care of the California Cotton & Factorage Company and Mr. McDevitt would O. K. it and I would charge it to him. All of the drafts so drawn were approved by Mr. McDevitt before they were paid. The indebtedness incurred by Pauley arose by the Cotton Company's taking a draft for \$12,000.00 which draft was dishonored.

Mr. West was occasionally in the office of the Cotton Company, probably once every ten days and he never did, that I know of, make any audit of the books and if he had made such an audit I think I would have known. West never made any examination of the books in my presence.

I made out the stock certificates in favor of Mr. Sears at the time of the transfer from Mr. West and was present when the alterations which appear on the stubs of the stock book were made.

The witness' attention was called to stub numbered 7. He testified that the word "cancelled" written thereon was written by Mr. Hartke and Mr. Hartke also wrote across the stock certificate "cancelled". I

(Testimony of James F. Norsworthy.)

personally made out the new certificates to Mr. Sears. They now bear date of May 24. They were not made out on that date.

“Q About when were they made?

A I couldn't tell you. They were made some time in the fall and I put the proper date on them, the date I issued them, and Mr. Sears said Mr. West wanted them dated back to May 24, and I erased them and dated them back.

Q So that the erasures appearing on the certificates were made by you?

A Yes.”

I also wrote “May 24” on the stubs corresponding to the five certificates that were issued to J. B. Sears. I cannot tell you what it was I erased, but I did enter there first the date on which I actually issued the certificates, whatever day that was. Then I erased that and dated it back to May 24.

Q Can't you turn to one of these others and tell what that date was?

A Well, I don't know whether I could or not.

Q Doesn't the figure there show the number of the month in figures, for instance, month “11” for November?

Well, this looks like two ones.

Q And an oblique line after it, followed by the date; isn't that what it looks like to you?

A It looks like that, yes. Yes, I erased that and dated it back.

MR. PARKE: We now offer in evidence these stock certificates, Mr. West having been unable to

(Testimony of James F. Norsworthy.)

produce the originals, and I take it the explanation as to the change has been satisfactorily shown.

MR. COSGROVE: It is stipulated that the same erasures appear on the originals as appear on the stubs as to the date.

MR. PARKE: Yes. And we ask that they be marked as Exhibit C; and also the stub of the stock register so far as the issue of other stock than that is concerned.

(Previously offered).

A portion of said Exhibits "B" and "C" is in words and figures as follows:

The following is a copy of one of the Certificates issued to J. B. Sears as contained in Defendants Ex. "B."

Incorporated Under the Laws of the State of California.

(Copy of:) THE GREAT SEAL OF THE STATE OF CALIFORNIA.

Number	Shares
--------	--------

13	100
----	-----

CALIFORNIA COTTON AND FACTORAGE  
COMPANY

CAPITAL STOCK \$100,000

PAR VALUE \$100 EACH

THIS CERTIFIES THAT J. B. Sears is the owner  
of One Hundred Shares of the Capital Stock of

CALIFORNIA COTTON AND FACTORAGE  
COMPANY

transferable only on the books of the Corporation

(Testimony of James F. Norsworthy.)

in person or by attorney on surrender of this Certificate properly endorsed.

IN WITNESS WHEREOF, the Corporation has caused this Certificate to be signed by its duly authorized officers and its Corporate Seal to be hereunto affixed

this 24th day of May 1920.

C. H. Hartke      CORPORATE SEAL      T W. McDevitt  
Secretary.                      of the                      President.

CALIFORNIA COTTON

and

FACTORAGE COMPANY.

(On reverse side:)

For value Received....hereby sell assign and transfer unto.....Shares of the Capital Stock represented by the within Certificate and do hereby irrevocably constitute and appoint.....Attorney to transfer the said stock on the Books of the within named Corporation with full power of substitution in the premises.

Dated.....19....

In Presence of.....

J. B. Sears

NOTICE. The Signature of this Assignment must correspond with the name as written upon the face of this Certificate in every particular without alteration or enlargement or any change whatever.

The following is a copy of Stubs of Certificate #2 and #13 as contained in Defts. Ex. "C"



(Testimony of James F. Nersworthy.)

## CERTIFICATE

No. 2.

(Cancelled \$5.00 U. S. I. R.  
Doc. Stamp.)

For 100 Shares

## ISSUED TO

T. J. West

(The word "Cancelled" appears  
written across the face of this  
certificate stub in ink, under  
which word is an erasure mark

DATED 9 1920 followed by the figures "1920.")

FROM WHOM TRANSFERRED

.....  
DATED.....19....

No. Original Certificate.	No. Original Shares.	No. of Shares Transferred.
.....	.....	.....
.....	.....	.....
.....	.....	.....

Received Certificate No.....

For.....Shares

this.....day of.....19....

## CERTIFICATE

NO. 13

For 100 Shares

## ISSUED TO

J. B. Sears

DATED May 24 1920

(Testimony of James F. Norsworthy.)

FROM WHOM TRANSFERRED

T. J. West

DATED.....19....

No. Original Certificate.	No. Original Shares.	No. Shares Transferred
3	100	100

Received Certificate No.....

For.....Shares

This.....day of.....19....

On the day of Mr. Sears' death I made no check to see how many tickets there were in the safe of the Cotton Company. The fluctuations in the cotton market during the period of the Company's operations was substantially as testified to by Mr. West. The monthly statements which I prepared reflected J. B. Sears' personal drawing account.

The end of the first fiscal year of the Cotton Company's operations was August 31 1920 and at that time I made entries in the books showing the closing of the books as of that date. It shows there was an operating profit of \$53,222.08. The books showed this profit was charged off to bad debts in the sum of \$63,068.12 and this deficit was carried over on the profit and loss debit to the next year. The net profit and loss from cotton operations—that is, the difference between the selling price and the buying price after deducting expenses—would be the net operating profit. There was an operating loss during the second year, but I have not balanced the books to ascertain how much it was.

(Testimony of E. F. Kramer.)

Testimony of

E. F. KRAMER,

a witness on behalf of defendant, who being first duly sworn, was as follows:

I am manager of the Southern California Claim Division of the Maryland Casualty Company. I know Mr. McDevitt. He called at our office about noon on May 19, 1921, in relation to the alleged loss under the bond in this case.

"A Mr. McDevitt called at the office about noon and stated he wanted a report on an occurrence that took place over at the California Cotton and Factorage Company. He said that the company had received notice from the Citizens National Bank that they had approximately \$140,000 worth of trust certificates. Mr. McDevitt told me that he then spoke to Mr. Sears about the matter and asked him, "How do we stand on this?" to which Sears made the reply, "Not very well". Mr. McDevitt stated that they then discussed the matter further—that is, he and Sears, and McDevitt said that he finally told Sears there was only two reasons for this, one of which is fraud, and he looked at Sears and Sears replied that maybe it was. They then talked the matter over still further and agreed to meet the following morning and go over the books and see just how the entire matter stood. Mr. McDevitt stated that he had known for some time that the Company had been losing money on account of the way the cotton market was going. He realized that Sears was worried, and when he, McDevitt, got

(Testimony of T. J. West.)

home that evening about nine o'clock he telephoned to Sears at his residence and they discussed this proposition over the 'phone. He told Sears not to worry any further, that they would meet in the morning, go over the books, and something would be done whereby Sears could straighten out the whole matter."

I told Mr. McDevitt that he should comply with the provisions of the bond, after he had referred to the bond, and I knew there was a provision in there that he should report immediately to the home office at Baltimore. Mr. McDevitt told me that the conversation he had with Sears was on April 28, at which time Sears told him the facts which he, Mr. McDevitt, related to me.

Witness

T. J. WEST

recalled by plaintiff for further direct examination.

The witness' attention was called to the minutes of the Cotton Company of May 20, 1920, at which action was taken regarding the resignation of Mr. Sears as Secretary of the Cotton Company, and the witness was asked if he recalled the occasion when that resolution was passed. The witness testified that as he recalled, the reason why Sears resigned was that he was going to be absent in Texas and New Orleans and in the East for some time. The Shepard & Gluck claim was also discussed, and the purpose of removing Sears as secretary was so that Shepard & Gluck could not get service upon Sears in the State of Louisiana in the event they started suit and attempted to serve him.



(Testmony of R. M. Farrar.)

R. M. FARRAR,

a witness on behalf of defendant, being first duly sworn, testified as follows:

DIRECT EXAMINATION

I have resided in Los Angeles for ten years and am a certified public accountant, working for myself. I have been in the government service as an auditor, in the income tax department.

It was thereupon stipulated that the witness was competent and qualified.

I was employed to audit the books and records of the Cotton Company shortly before the trial of this action and subsequent to the time they were audited by Mr. Bailey. The books and records which I examined are those here in court. I did not see the book which Mr. Norsworthy has described as "stock book", and I did not see the trial balance book which Mr. Norsworthy testified was kept. I prepared a statement as a result of my audit. Which statement or report was thereupon introduced and received in evidence as defendant's Exhibit "E." The following facts set forth in said report are stipulated, to-wit:

"It is stipulated that between the 19th day of November, 1920, and the 25th day of April, 1921, eighty-seven (87) sight drafts were accepted by J. B. Sears, and that said eighty-seven (87) acceptances are in the total amount of Eighty-two thousand, four hundred eighty-seven 96/100 (\$82,487.96) Dollars. That between said 19th day of November, 1920, and the 1st day of December, 1920, twenty-five (25) of said

(Testmony of R. M. Farrar.)

eighty-seven (87) sight drafts were accepted by J. B. Sears, and that said twenty-five (25) acceptances are in the total amount of Twenty-nine thousand, three hundred thirty-seven 99/100 (\$29,337.99) dollars. That attached to said eighty-seven (87) sight drafts were fourteen hundred seventy-six (1476) warehouse receipts for fourteen hundred seventy-six (1476) bales of cotton, and that attached to said twenty-five (25) sight drafts were four hundred fifty-five (455) warehouse receipts for four hundred fifty-five (455) bales of cotton. That between said 19th day of November, 1920, and said 25th day of April, 1921, plaintiff delivered to said J. B. Sears said fourteen hundred seventy-six (1476) warehouse receipts, and accepted therefor eighty-seven (87) trust receipts, and between said 19th day of November, 1920, and said 1st day of December, 1920, plaintiff delivered to said J. B. Sears said four hundred fifty-five (455) warehouse receipts and accepted therefor twenty-five (25) trust receipts. That upon the death of said J. B. Sears said California Cotton & Factorage Company had in its possession and thereafter surrendered to said Citizens National Bank three hundred eighty-five (385) of said fourteen hundred seventy-six (1476) warehouse receipts. That seventy-six (76) of said three hundred eighty-five (385) warehouse receipts so surrendered were originally attached to said twenty-five (25) sight drafts accepted by said J. B. Sears between said 19th day of November, 1920, and said first day of December, 1920, and that said seventy-six (76) ware-

(Testmony of R. M. Farrar.)

house receipts had been delivered to said J. B. Sears by said Citizens National Bank between said 19th day of November, 1920, and said 1st day of December, 1920. That said four hundred fifty-five (455) bales of cotton cost said California Cotton & Factorage Company at the time of its purchase, and was then of the value of Twenty-nine thousand, three hundred thirty-seven  $99/100$  (\$29,337.99) dollars. That said three hundred eighty-five (385) bales of cotton at the time of its purchase cost said California Cotton & Factorage Company, and was then of the value of Twenty-one thousand, eight hundred ninety-three  $34/100$  (\$21,893.34) dollars. That said seventy-six (76) bales of cotton at the time of its purchase cost California Cotton & Factorage Company, and was then of the value of Five thousand, fifty-six  $02/100$  (\$5,056.02) dollars.

That upon the death of said J. B. Sears, said California Cotton & Factorage Company did not have in its possession and did not thereafter surrender to said Citizens National Bank ten hundred ninety-one (1091) of said fourteen hundred seventy-six (1476) warehouse receipts. That said ten hundred ninety-one (1091) bales of cotton represented thereby cost said California Cotton & Factorage Company at the time of its purchase, and was then of the value of Sixty thousand, five hundred ninety-four  $62/100$  (\$60,594.62)."

The books of the Cotton Company appeared to have been kept in the regular manner. The audit made was



(Testmony of R. M. Farrar.)

several months after the business had been closed, and the records, of course, were in a very mixed condition, and it was very hard to audit the accounts. The books had been moved from one office to another, and of course in changing about from place to place they had become confused, one with the other, and it was difficult to gather the books all together. The books of the Cotton Company show that during the first year of the Company's operations, that is beginning in 1919 and ending August 31, 1920, there was handled 92 of the Cotton Company's acceptances by the Citizens National Bank, all of which were paid by the Cotton Company. It was thereupon stipulated that all of the acceptances of the Cotton Company handled through the Citizens National Bank during the first year of the Cotton Company's operations were paid, and that 76 of the acceptances handled during the second year of the Cotton Company's operations were paid. The acceptances of the Cotton Company which were handled through the Citizens National Bank during the first fiscal year of the Cotton Company's operations was \$95,640.83, and the total of the 76 acceptances which were paid through the bank by the Cotton Company during the second year aggregated \$115,593.28. All this was in addition to the \$82,000.00 of acceptances held by the bank which were not paid. I found among the records and files of the Cotton Company a large number of acceptances stamped "paid", to all of which were attached trust receipts. I found there was no change in the way in which the Cotton Company's books were kept during



(Testmony of R. M. Farrar.)

the first year as compared with the second year, and the books do not indicate that the business as between the Cotton Company and the bank, that is, the manner of transacting business, was changed at any time during the period the Cotton Company operated.

From my examination of the books I did not find any financial transaction of the Cotton Company which had not been properly entered. At the time I examined the books a number of entries had been made by Mr. Bailey covering transactions subsequent to Mr. Sears' death. There was also entered the \$26,000.00 item and sundry other entries which had reference to the loan accounts. Aside from the entries in relation to the loan account I did not find any financial transactions which were not entered in the books. I checked the books to see whether or not proper entries were made of all withdrawals of money and deposits of money, checking the bank's statements, which were delivered to the Cotton Company every month, with the drafts that had been drawn to see that they had properly been deposited to the Company's credit. I found that all of them had been. I also made a check of the cotton purchased by the Cotton Company during the second year. I secured this information from the buyers' reports principally and from the account sales. The buyers' reports contained data as to each and every bale of cotton by descriptive number. I also checked as to what was done with all cotton purchased during the second year, and I was able through the books to find a record of every bale of cotton

(Testmony of R. M. Farrar.)

that had been purchased. There were seven bales that were on hand that there was no record of the purchase of, and it was afterward determined to be a consignment from Dr. Reeves. There was no record of that. The books all contain a record by descriptive number of each and every bale of cotton covered by the trust receipts. I was able to identify each and every bale of cotton covered by the trust receipts through the buyers' reports, which had a memorandum thereon that the cotton therein listed is covered by an acceptance of a certain number, and in that way I could ascertain the cotton covered by any particular acceptance. I found trust receipts bearing serial numbers corresponding with the serial number on each of the acceptances, and I found that the number of bales of cotton referred to or entered upon the trust receipts corresponded with the number of bales of cotton that appeared on the face of the acceptances, and then by going to the buyers' reports I was able to get the descriptive number of the bales of cotton covered by the particular acceptances. I was thus able by the buyers' report and the acceptance account to check by descriptive number each and every bale of cotton purchased, and I was able to check by descriptive number each and every bale of cotton that was sold, with the exception of 32 bales, concerning which there was a confusion in the numbers, the numbers being obliterated. The numbers are painted on the cotton in a great many instances with a marking pot and they are obliterated from time to time, and the num-

(Testmony of R. M. Farrar.)

bers become confused in changing from compress to cotton tickets.

I received from Mr. Bailey the information as to the number of cotton tickets still on hand at the time of Mr. Sears' death. As I recall there was some 387 tickets. The records of the Cotton Company show the sale of all the cotton, except that which was represented by the tickets on hand, and from the records submitted to me I was able to ascertain to whom the cotton was sold and how much was realized from the sale of it. The record of moneys received from the sale of cotton as entered in the books corresponded with the entries in the bank deposit book. I compared the sale price of the cotton by the Cotton Company during the second year, with the purchase price, and found there was an average of about \$12.00 a bale loss, that is; the gross selling price was about \$12.00 a bale less than the gross purchase price. That would be averaging it for the period of the second year.

I was present in court and heard Mr. Bailey's testimony in relation to the opening up of what he would designate as a "trust account". In my opinion it was not necessary to have such a "trust account" in order for the books to reflect the true financial condition of the Cotton Company, for the reason that the asset was on the books in a total amount, in the total of the acceptances. It was placed on the books in full. The placing of such an account on the books would merely show the difference between what the unpaid acceptances amounted to and the amount of cotton on



(Testmony of R. M. Farrar.)

hand in the office. It would not increase or decrease the liability of the Company to the bank, and such an account as Mr. Bailey indicates would have duplicated entries contained in the acceptance account. To reflect the liability of the Cotton Company to the bank for trust cotton it would have been necessary to have an account opened in the books showing the amount of the cotton tickets obtained from the bank that were not sold. An account would have had to have been opened up charging trust cotton with the amount of tickets received and crediting that account with the amount of cotton covered by those tickets that were sold. Such an account would reflect the same liability as the acceptance account. So far as liability is concerned the only difference would be that the "trust cotton account" would reflect the market price in the cotton sold, but to keep such an account it would be necessary to price the cotton you had on hand every night according to the market price, and you would have had to make adjusting entries with each fluctuation in the market.

Whereupon the witness was exhibited certain documents, being acceptances number 13 and number 16, dated in September and October, 1920, and asked whether or not any buyers' reports were attached thereto, and concerning that matter the witness testified:

The buyers' report is the last document attached to the acceptance which you have handed me. These buyers' reports contain the statement of the number of bales, the individual numbers of the bales, the



(Testmony of R. M. Farrar.)

weight, the price at which it was bought and the total amount, as well as the party from *him* it was bought. The entry thereon "B. R. No. 7" indicates buyers report No. 7, and the entry "A/C, No. 16" indicates the number of the acceptance, and I find that the acceptance attached thereto is number 16 and that the trust receipt attached thereto also bears the same number 16. This buyers' report covers eight bales and the acceptance and trust receipt attached thereto each cover eight bales. The entry "St. B. No. 147" appearing upon the buyers' report indicates that it was entered in the stock book. The reference to the acceptance account as contained in the books of the Cotton Company disclosed that said acceptance number 16 is entered therein with the information as to the number of bales of cotton covered thereby, the amount of the acceptance, the date of purchase, and such account also shows the acceptance was paid on November 29, 1920. I find that similar entries were made in the acceptance account concerning each and every acceptance that was paid, taking the eighty-seven acceptances that were not paid, regarding entries on the credit side, there are no entries at all. I can from the acceptance record alone ascertain the number of bales of cotton covered by the acceptances which were unpaid at any particular date. I would do this by merely counting the number of bales that were covered by acceptances that were not paid. The figures on the acceptance record appearing under the heading "Bales", opposite each acceptance number, indicates the number of bales of cotton covered by that unpaid

(Testmony of R. M. Farrar.)

acceptance, and to ascertain the total number of bales covered by acceptances would require that only these numbers be totaled up. For instance, on the unpaid acceptance number 109, the record shows that it covered eleven bales of cotton. You could ascertain from the cotton sold book or from the stock record book whether that eleven bales of cotton covered by acceptance number 109 had been sold and disposed of. The descriptive number of the eleven bales covered by acceptance 109 could be ascertained from the buyers' report, and having obtained the particular descriptive numbers of the eleven bales, then by referring to the stock book you might ascertain whether any of the eleven bales were on hand or had been disposed of. Thus it would have been possible by check of the books at any time to ascertain the number of bales of cotton covered by unpaid acceptances, and I could have ascertained at any time what portion of the cotton covered by unpaid acceptances was on hand and what portion had been sold. That information could have been obtained from the stock book.

"Q BY MR. PARKE: Can you determine, Mr. Farrar, from an inspection of the books submitted to you, that the Cotton Company was selling cotton covered by acceptances and trust receipts held by the Citizens National Bank?

A Yes sir."

I could do that by resorting to the account sales, and by tracing the numbers from the purchase book to the cotton sold book, and the items not marked off

(Testmony of R. M. Farrar.)

would show unsold cotton. Those that were marked off would show the sold cotton. Then I would connect the sold cotton up with the unpaid acceptances and trust receipts held by the bank by the numbers of the bales. The cotton purchase book detailed the buyer's reports in number; the cotton sold book detailed the bales of that cotton. Now from the cotton purchased you would mark off those which were sold from the cotton sale book, and the difference would be the unsold cotton. I could ascertain whether any of the cotton so sold was covered by unpaid acceptances held by the bank by the ticket numbers covered by the acceptances. To connect up with the ticket numbers with any particular acceptance would have to be in a great deal of detail. The cotton sold book detailed the sale of the cotton, and the stock book detailed the sale of the cotton covered by acceptances. The information connected up with cotton sold with any particular acceptance. Taking this particular cotton covered by acceptance number 16: Acceptance number 16 covers eight bales. I can indicate where in the books there is a record of the sale of those particular bales of cotton. The sale would be in the cotton sold, and a reference would be made to the sake in the stock book, showing those individual bales that had been sold. By comparing the sales with the buyer's report corresponding in number to the acceptance, you could tell by the number on the bale whether that particular cotton belonged to a particular acceptance or not.



(Testmony of R. M. Farrar.)

From examination of the books it could have been ascertained that moneys received from the sale of cotton covered by unpaid acceptances held by the plaintiff bank was being used for purposes other than the payment of these acceptances. I could do that by the checks which were drawn. The deposit was made to current account and the money was used for different purposes, and could be determined by the stub of the check book.

It was thereupon stipulated that save and except for the bales of cotton on hand, all of the cotton which is unaccounted for to the bank was sold and out-bound documents deposited in the checking account.

The books of the Cotton Company disclosed that the money received by the Cotton Company from the sale of the cotton covered by the unpaid acceptances at the bank was deposited in the current account of the Company in the plaintiff bank, and that thereafter it was all applied in payment of operating expenses and in payment of acceptances, save and except the amount charged to Sears' personal account.

The total amount of acceptances of the Cotton Company handled through the plaintiff bank and paid from the time the Company started business up to April 30, 1921, was \$1,156,720.12. It was thereupon stipulated that all of these acceptances that were paid to the plaintiff bank, were paid by checks of the Cotton Company drawn on its checking account in plaintiff bank.

The records of the Cotton Company show that of the whole \$1,156,720.12 of acceptances which were



(Testmony of R. M. Farrar.)

paid, were paid by check, and no part thereof paid by deposit in the note department of "outbound documents". Acceptances were paid from time to time during the whole period of time by checks covering one or more acceptances, and that manner of payment continued during the whole period of the company's operations as is shown by the books there.

In checking the books and records of the Cotton Company I did not find any false entries, and I balanced the books as of the date of the close of business and they balanced within ten cents.

Had the outbound documents covering cotton sold been deposited directly in the note department to be credited on unpaid acceptances, there would be a way in which the company could have kept a record of its cash transactions. It would have been done by a journal entry. It is not the usual and customary way of handling cash transactions, through journal entries. The journal entry would have had to be made, charging the bank with the money and crediting the acceptances. Q. And that account would have been duplicated, practically, by the acceptance account, would it not? A. Well, the acceptance account would have shown the difference all the time, of unpaid acceptances, of course.

"Q I think you testified yesterday that in your opinion it was unnecessary in order to reflect the true financial condition of the Cotton Company that a trust cotton account such as indicated by Mr. Bailey be opened up; and I understand you desire to make an additional statement as to why, in your opinion,

(Testmony of R. M. Farrar.)

that would not be necessary. Will you at this time make such statement to the Court as to why you consider such an account unnecessary.

A The question of the trust account may cause some reflection as to why the principles of accounting couldn't be applied to that particular account. In other words, in creating the trust account it would duplicate the acceptance account from the standpoint of the deposit. From the standpoint of the credit side the trust account was created by an arrangement to either replace the tickets or to return the funds from the sales of cotton. On the return of the tickets, or the return of the proceeds from the sale of cotton if the trust account had been set up, there would have been a difference between the two, whereas the acceptance account would not have shown the same results, the difference being the cotton sold which had not been paid for under the acceptances. If this account had been adjusted from time to time by taking up the difference between the cost of the cotton covered by the acceptances and the proceeds of the sale, the effect of the account would have been entirely lost; it would be just the result of the number of tickets they have. If it had not been, the account, when it was closed out, had the cotton been sold at a loss,—there would have been an item in the trust account with no tickets on hand and no funds to cover it.

Q That is, if all the cotton had been sold and the proceeds been—

(Testmony of R. M. Farrar.)

A If all the cotton had been sold and the proceeds of that sale of all the cotton had been less than the acceptances, there would have been an asset on the books for the cotton in trust and no tickets on hand and no proceeds to pay the account, because of their having been turned in. When the cotton tickets were returned, or the proceeds of the sale, the trust would have been extinguished, but not so on the books, unless the account had been adjusted.

Q Then, as I understand you, if all the tickets received from the Bank had been sold and the total proceeds from the sale thereof returned to the acceptance window, since the cotton was sold for less than it was purchased for, there would have been an apparent liability appearing on the books.

A Yes sir.

Q Although by the return of the total proceeds the trust account would have been extinguished?

A Yes sir; and there would still be a liability on the books for the amount of the unpaid acceptances.

MR. COSGROVE: Even after you have paid them?

A If the proceeds did not equal the total payment.

Q BY MR. PARKE: If the proceeds from the sale of cotton had equaled the amount of the cost of the cotton what would have been the result?

A Then the acceptance account and the trust account would have been in balance all the time.

Q And would have been synonymous as to entries?

A Yes sir, and would have been duplicated."

(Testmony of R. M. Farrar.)

Thereupon there was offered in evidence certain buyers' reports attached to acceptances No. 13 and No. 16, said buyers' reports being marked as defendant's exhibit F, and one of which reports together with draft and trust receipt attached is as follows:

(Defendant's Exhibit F)

COTTON DRAFT

13

No. 606

California Cotton & Factorage Co.

COTTON (Stamped in blue  
ink) 19095

LOS ANGELES, CALIFORNIA

Sept 27th 1920

At Sight.....PAY TO THE ORDER OF  
E. G. Caruthers State Bank.....\$1453.32  
Fourteen hundred fifty three and 32/100....DOLLARS  
VALUE RECEIVED AND CHARGE TO AC-  
COUNT OF

A/C OF 13 B/C-MARKED Various

B/L No. 13

B/C ATTACHED 6525

or

TOTAL WT.

W. H. Rept.

TO California Cotton & Factorage Co.

Los Angeles, Calif.

T. W. Ewing

(Stamped across face in green ink):

Date SEP 30 1920

ACCEPTED

CALIFORNIA COTTON & FACTORAGE CO.

By J. B. Sears

Manager



(Testmony of R. M. Farrar.)

Thu. CITIZENS NATIONAL BANK

LOS ANGELES, CALIF.

(Stamped across face in purple ink):

P A I D

NOV 29 1920

NOTE TELLER

CITIZENS NATIONAL BANK

LOS ANGELES, CAL.

(Stamped on reverse side):

Pay to ANY BANK OR BANKER

E. G. CARUTHERS STATE BANK

91-97 Somerton, Ariz. 91-97

R. H. RAMSEY, Vice-President

and Cashier

(Defendant's Exhibit F)

TRUST RECEIPT

No. 13

CALIFORNIA COTTON & FACTORAGE CO.

COTTON

LOS ANGELES, CALIFORNIA. SEP 30 1920

RECEIVED IN TRUST FROM THE

The Citizens National Bank of Los Angeles BANK  
OF LOS ANGELES DOCUMENTS, DESCRIBED  
BELOW, THE PURPOSE BEING TO SECURE  
DELIVERY OF THE SHIPMENTS AND SECURE  
OUTBOUND DOCUMENTS THEREFOR, WHICH  
SHALL BE RETURNED TO SAID BANK IN  
CANCELLATION OF THIS RECEIPT.

B/L NO.....NO. B/C....13....MARK.....

COMPRESS OR YARD RECEIPTS....13....B/C  
ATTACHED

1453.32

CALIFORNIA COTTON & FACTORAGE CO.

J. B. Sears MGR.

(DEFENDANT'S EX. F)  
No. Bales 13 Pur. No. —

INVOICE OF COTTON  
BOUGHT FOR ACCOUNT OF  
CALIFORNIA COTTON & FACTORAGE  
COMPANY

COTTON LOCATED AT  
ABBOTTS COTTON YARD 13 B/C  
Compress — B/C  
COTTON SHIPPED AS FOLLOWS COTTON MARKED

Somerton, Ariz. California Sept 27th 1920  
THIS COTTON REPORTED AS FOLLOWS

DATE	BUYER'S REPORT	NO. NO.	BALES	LIMIT DIF. B/M	BALES YET SHEET TO INVOICE	SHIPPED TO	B/L NO. NO. BALES
------	-------------------	------------	-------	-------------------	-------------------------------	---------------	----------------------

6	13	22½					
---	----	-----	--	--	--	--	--

MARK  
BLOCK  
/ /  
CALCU-  
LATION  
O.K.  
Limit O.K.

BALE OR	BALE OR	BALE OR	BALE OR
TAG NO. WEIGHT PRICE AMOUNT	TAG NO. WEIGHT PRICE AMOUNT	TAG NO. WEIGHT PRICE AMOUNT	TAG NO. WEIGHT PRICE AMOUNT

1093	510		
1108	465		
1128	535		
1304	535		
1332	535		
1344	530		
1357	530		
1369	475		
1394	540		
1395	520		6525
1437	435		22½
1457	512	22½	1377.45
1520	403	22½	90.67
			13050
			146812
			1625
			145187
			145

1453 32  
(Stamped as follows):

B. R. No.	6
A/C	
Ck. No.	13
C. S. No.	1
Pur. No.	23
L. F. No.	23
St. B. No.	146
O. K.	F

(Blue pencil):  
Fix in Box 13

RECAPITULATION INVOICE

MARK	Bales	BOUGHT FROM	WEIGHT	PRICE	AMOUNT
JPT & BB	12	J. P. Taylor & Bunton Bros.	6122	22½	1377.45
GK	1	Georgina Klindera	403	22½	90.67
					1468.12
					16.25
		Less Yardage			
13		TOTALS	6525		1451.87
					1.45 ex.

(Stamped): NOTED J. S. B.

CHARGES (IF ANY) TO BE PAID BY US ON ABOVE

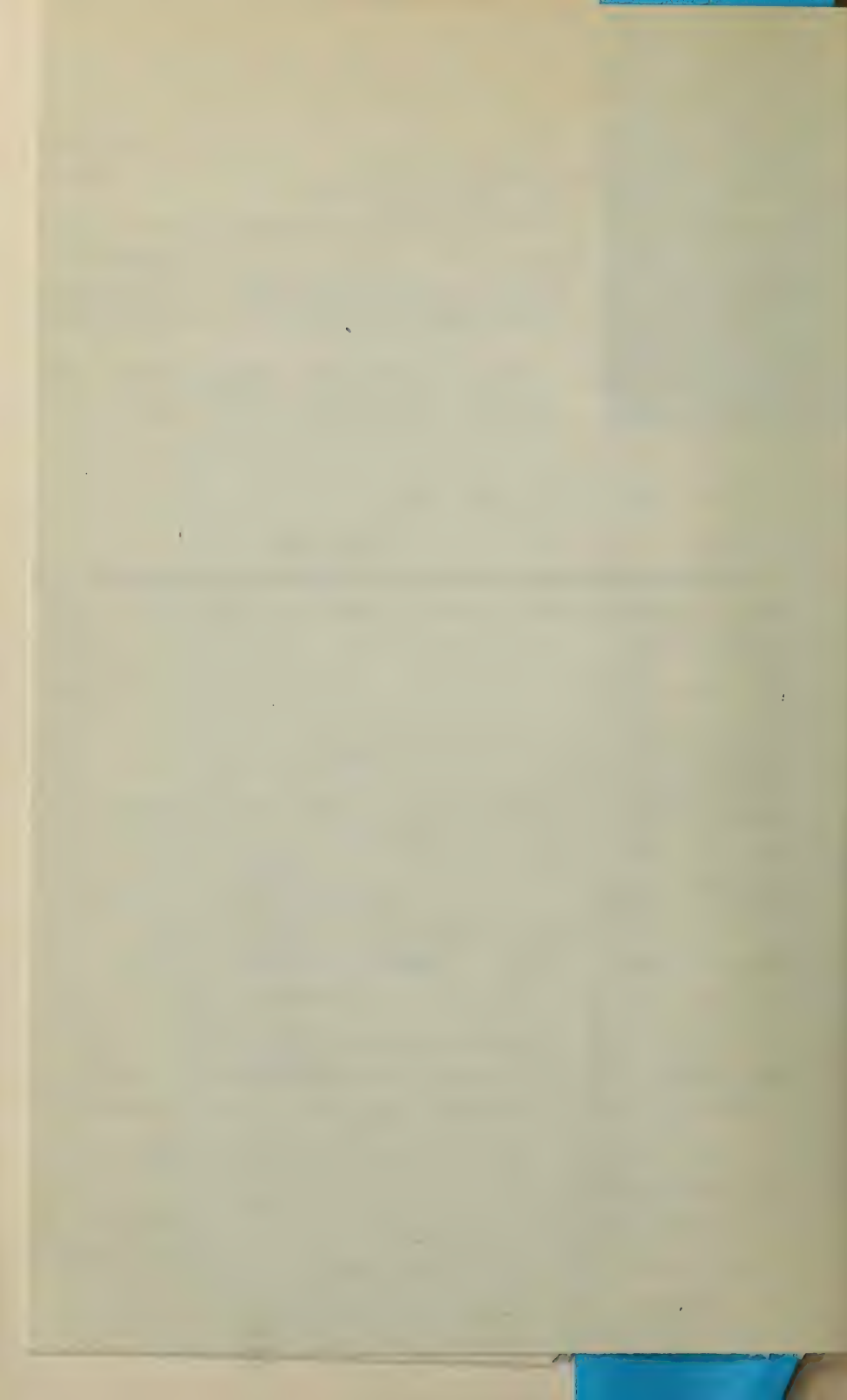
Charges for Yardage.....  
On 13 Bales Cotton, @ 125 per bale \$1625

PAID FOR

By Draft No. 606 for \$1453.32  
Drawn on Agency at Los Angeles  
California  
Favor of E. G. Caruthers State Bank  
T. W. Ewing.

Note:—

(Other portions of said Exhibit "F" consisting of cancelled checks and pencil memorandums are not copied into the Bill of Exceptions)



(Testmony of R. M. Farrar.)

### CROSS EXAMINATION

I have had twenty years experience. I made a careful analysis of the books of the Cotton Company in preparing my report. I worked on the books over a period of about six weeks. I am admitted to practice as an attorney. The witness' attention was called to his report, defendant's Exhibit "E", and particularly a portion thereof given on page 20, which reads as follows:

"The system of accounting in use by the corporation was very inadequate, and the manner of keeping its records was most careless. Information as to details is lacking, and employes apparently have little knowledge even as to general conditions. Only meager memorandums have been made in explanation of most entries, and numerous assets and liabilities were never recorded in the books of account until an audit was made about April 30, 1921."

and also on page 18:

"The affairs of the corporation were in a state of chaos."

and the witness was asked whether or not at this time he wished to make any explanation to the court of his statement to Mr. Parke yesterday with reference to the completeness of these records and these statements that appear in the report, and to which the witness testified:"

That by chaotic condition of the books he meant that from the records it was very hard to determine the general course, the books having been removed



(Testmony of R. M. Farrar.)

from the office of the Company. The minute book, stock book and trial balance book were not available, and I had to use the book Mr. Bailey had used in determining the sale of cotton by individual number. The witness' attention was also called to page 15 of his report, wherein is set forth the following:

"An attempt has been made to account for the purchase and sale of each individual bale of cotton, and this has been found impracticable with the inadequate system of accounting and the meager information in the office. Some explanation no doubt should be made as to why this cannot be done, and further detail as to the handling of cotton will be given."

Also to page 34 of the report, under the heading "Accounting of Cotton by Individual Sales", wherein is set forth:

"An attempt was made to account for each bale of cotton by individual number and weight, but this was not found practical owing to the lack of information in the records as to change of number of bales, etc." And the witness was asked to make any explanation of said statements in the light of his testimony, to which the witness answered:

That by way of explanation I will say that this reference made to page 15 was found impracticable with the inadequate system of accounting for the reason that the change of the numbers and bales had not been kept. They should have been kept either by the buyers in the field, when the changes were made in the compress, and reported to the office; in

(Testmony of R. M. Farrar.)

other words, they should have been kept by somebody connected with the California Cotton and Fac-torage Company."

I never saw the stock record book that was kept by the Cotton Company, and never had any access to it. So that in my accounting I would not have access to the book that I referred to in that answer. The buyers report shows the data given on the stock book, where it could be obtained.

Thereupon the witness' attention was called to page 13 of his report, as follows:

"In the sale of cotton it would be sold by grade, and it will therefore be seen that any sale might include bales of cotton purchased at different times and covered by many acceptances. In order to permit this it would be necessary to obtain from the Bank the bale tickets covering the grade desired, and this was done by substituting a trust receipt for each bale ticket so obtained."

Concerning this statement the witness testified:

This report was made after I had completed my audit. In answer to the question as to whether after I had completed my audit I understood that a trust receipt was substituted for each bale of cotton, by way of explanation I will say that I commenced this audit in October and there was nothing so far as these trust receipts—except those I examined in your office—and the information as to these, as to how this transaction took place, was given me by Mr. Bailey, and that was my understanding that I received from

(Testmony of R. M. Farrar.)

him at the time I made the audit. So that at the time I made this audit and made this report I thought there was a trust receipt given for each bale of cotton."

The witness' attention was also called to page 14 of his report, as follows:

"To secure the Bank against any loss by releasing the bale tickets a special deposit was made to the Citizens National Bank of \$26,000, and this amount was advanced by T. J. West Company, Calexico, California."

And in relation thereto the witness said that he had later ascertained since preparing the report that the \$26,000.00 did not have anything to do with the acceptance and trust receipt accounts, but that it was a special account, separate and distinct. That is another phase of the information that I got from Mr. Bailey on checking the books. I ran across where this had been cut out, and that is why I asked how it had been done. It was thereupon stipulated that the entry in the books regarding the \$26,000.00 was made by Mr. Bailey; that is, the entries which now appear in the books regarding the \$26,000.00 item were made by Mr. Bailey.

The witness' attention was also called to page 14 of his report, as follows:

"After the sale of cotton it was planned to take up the acceptances at the Bank or to cover at least such portion of it as was cotton withdrawn."



(Testmony of R. M. Farrar.)

Concerning this the witness testified that he had since discovered that that was not the plan, but that the plan was to pay acceptances by check and to pay several acceptances at the same time, a considerable period of time after the cotton was sold.

The witness' attention was further called to page 14 of his report, under the head "Loan Cotton", as follows:

"In addition to purchasing cotton the corporation contracted for the raising of cotton. Amounts were advanced for seed, cultivation and picking, and the crop of cotton was taken in settlement."

and concerning this the witness testified that he was not positive whether this plan was followed during both years of the Cotton Company's operations, but a considerable loss resulted to the Cotton Company from those contracts for the raising of cotton.

And on page 17 of my report, the last paragraph but one I stated: "From exhibits of sales it will be seen that the proceeds of all sales were deposited to the credit of the Company either in the Calexico National Bank, Calexico, California, or Citizens National Bank of Los Angeles". They put some sales thru the Calexico National Bank.

The statement set forth on page 18 of my report is correct—which statement is as follows:

"The statement, as reflected by the records of the corporation, discloses that a gross profit was made on cotton for the fiscal year ending August 31, 1922, of \$53,222.08. This amount is reduced by the amount of



(Testmony of R. M. Farrar.)

expenses, \$23,507.45, and leaves a net profit of \$29,714.63. Bad debts are charged off to the amount of \$63,068.12, and taking this item into consideration the loss for the year sustained by the corporation is \$33,353.49."

My report shows that from the entries appearing in the books of the Cotton Company at the time I audited them, which entries included those made by Mr. Bailey, there appeared an overdraft on Mr. Sears' personal account of \$5,508.00.

The witness' attention was called to page 27 of his report, as follows:

"I hereby certify that in my opinion the accompanying balance sheet reflects the true condition of the corporation as of July 1, 1921, except for the liability of cotton oversold." That statement was my opinion at that time. I checked every one of the documents marked defendant's Exhibit F which are attached to two acceptances that were accepted on October 4 and September 30, 1920, respectively. But I have no particular recollection of these two individually. In the matter of these different documents that are attached to these acceptances, I do not know anything about when they were attached to them or who attached them to them. The acceptances, which is the first instrument in the files, is the ordinary acceptance that came into the bank with the cotton tickets attached. And it does not differ from any of the other acceptances that came in. The trust receipt that is attached to the acceptance is the form of receipt that

(Testmony of R. M. Farrar.)

was used by the Cotton Company when they took the ticket from the sight draft and substituted a trust receipt for it.

I do not know the significance of the telegram blank upon which appears some penciled notations, and I do not know what connection the four checks attached thereto have, but the last document attached to the exhibit is a buyers' report. It is the form of report that was gotten up in the field by the employed buyer of the Cotton Company at the time he made the purchase of cotton, and when he bought the cotton the cotton tickets and the sight draft came through to the plaintiff bank and the buyers' report came through the mail to the Los Angeles office of the Cotton Company.

I do not know where the green ink stamp was put upon the buyers' reports, wherein appears certain numbers which furnish certain data. I do not know whether this stamp and information was put on the buyers' report after it reached the local office or not, but I think it was supplied here.

"Q Now let me show you this acceptance account, and calling your attention to No. 77, of date November 19, 1920, which appears to be the first one not paid, I would like to have you state to the Court how you could determine from the books or records of the California Cotton & Factorage Company whether or not the bank held a trust receipt for that cotton (handing book to witness).

(Testmony of R. M. Farrar.)

A The only way I could tell from this would be on the buyers report.

Q All right; I will show you a buyers report and would like to have you indicate to the Court—taking the ones that have been introduced in evidence—anything that indicates that a trust receipt was ever issued (handing paper to witness).

A This calls for acceptance account in the Calexico Bank of 25 bales of cotton. (Examining buyers report)

A This is shown by an acceptance number on here, on this buyers report.

A I don't know what further answer I could make on this. The buyers report indicates the total cotton sold and the acceptance number."

The buyers' reports do not say anything about trust receipts. I obtained my list of trust receipts outstanding on July 1, 1921, and the amount of them, from the bank records.

#### REDIRECT EXAMINATION.

I did not have to go to the bank records to get the number and the descriptive identification of each and every bale of cotton covered by unpaid acceptances, but I did, after completing my report, which has been introduced in evidence, prepare for use in court a statement showing the history of each and every bale of cotton covered by the 87 unpaid acceptances. The report which I prepared shows the disposition of the cotton covered by the unpaid acceptances and where the cotton came from, and it identifies by descriptive



(Testmony of R. M. Farrar.)

bale number each and every bale of cotton covered by unpaid acceptances, and it shows whether the same was sold or is still on hand, the sale number and the invoice number. All of this informataion was obtained from the books and records of the Cotton Company without reference to the record kept by the bank, except that I may have obtained some of the information from the trust receipts, but I was able without regard to the trust receipts and from the books kept by the Cotton Company to trace the disposition of each and every bale of cotton that was sold, and that without reference to the accounts kept over at the plaintiff bank.

Whereupon the report so prepared by the witness was offered and received in evidence as defendant's Exhibit G, which said exhibit consists of approximately 19 pages, and it is stipulated that said report has entered thereon what the witness testifies is a full and complete history of each and every bale of cotton covered by the unpaid acceptances and trust receipts held by the plaintiff bank at the time of Sears' death, showing the source from which cotton came, when it was sold and the amount realized therefor, and also the identical bales of cotton belonging to each and every acceptance and trust receipt, identifying each bale by its bale number and showing whether it had been sold and disposed of or was still on hand. In the preparation of this schedule marked defendant's Exhibit G, I used the book gotten up by Mr. Bailey in preparation of some of the data. Concerning



(Testimony of J. F. Norsworthy.)

the stock certificate book I find that the stub for certificate number 18 has been removed from the book. My recollection is that when I first examined the stock certificate book there was one share made out to T. J. West unsigned by the president of the Cotton Company.

J. F. NORSWORTHY,

a witness recalled by defendant, testified as follows:

The documents which have been introduced in evidence as defendant's Exhibit F are what I refer to as buyers' reports. The information, that is, the various letters and figures thereon, was placed there by me; that is the numerals appearing after the green stamp. The Company had a rubber stamp which I put on when I received the buyers' reports through the mail. I got the information which I entered thereon from the buyers' report, which indicated the number of the acceptance given for the cotton covered by that particular buyers' report. The entry "C S No. 1" means cotton sales sheet, and "Pur. No." indicates the office purchase number, and "L F No." means ledger folio number, and on the ledger folio was entered the total amount of the cotton and the weight. It was not the general ledger, but the consignment ledger. The entry "St. B. No." means stock book number, and on the page of the stock book so indicated would be given the acceptance number, the bale number and the weight of the bales, and it would give the descriptive number of each bale.

(Testimony of J. F. Norsworthy.)

I never at any time talked to Mr. Sears as to what I should do in the way of depositing outbound documents. The first time I went to the bank with an outbound document I went to the receiving teller's window to make a deposit. He told me I would have to see one of the vice presidents to get it O. K.'d, so I went over and got the vice president to O. K. it but I never received any instructions from Mr. Sears in that particular. The reason I took the outbound document to the receiving teller's window is because that is our custom in Texas; whenever we have anything to deposit we go and give it to the receiving teller; we don't have to have it O. K.'d. That is our custom whether the cotton being sold was covered by trust receipts or not. I worked with the Planters' Cotton Oil Company and with the Choctaw Oil Company.

#### RECROSS EXAMINATION

The information which I put into the stock book I took from the buyers' report, and everything except the classification of cotton that appeared in the stock book appeared on the buyers' reports.

When drafts came in against the California Cotton and Factorage Company for expenses in connection with the raising of cotton in the San Joaquin Valley I would advise Mr. McDevitt and have it O. K.'d by him, or if he was not present would telephone him and get his authority to pay the draft, and I would then charge it to the McDevitt Cotton Company account and pay the draft by check. These drafts were

(Testimony of Thomas W. McDevitt.)

paid by checks signed by J. B. Sears, if he was in the office, otherwise by myself. The other cotton loans were all handled in the same manner. The Shepard & Gluck claim against the Cotton Company was for alleged shortage in weights and grades.

#### REDIRECT EXAMINATION

After entering in the stock book the information contained in the buyers' report, I would later, when the cotton was sold, make entries in the stock book, marking off the cotton sold and the date it was sold. The confusion in a few instances of the identifying number of the bales of cotton occurred in this way—the cotton would be concentrated at the compress, where the yard tickets would be surrendered and compress tickets issued in lieu thereof, and some times several bales would go into one compress, but by the stock book we could trace the identical number of each bale of cotton. We had to keep it that way.

Whereupon the defendant rested its case.

THOMAS W. McDEVITT,

a witness on behalf of plaintiff, was recalled.

#### DIRECT EXAMINATION

It is not true that, as testified by defendant's witness Cramer, in talking to Mr. Cramer of the Maryland Casualty Company on the 19th day of May, 1921, that I told him that the Citizens National Bank had approximately \$140,000.00 worth of trust certificates. I told him the bank held acceptances. It is not true that, as testified by defendant's witness Cramer, I told

(Testimony of C. H. Hartke.)

Mr. Cramer that I had known for sometime that the Cotton Company had been losing money on account of the way the cotton market was going. I did not make any such statement.

Pursuant to stipulation the testimony of C. H. Hartke, given at the first trial of this cause, was read into evidence, no objections appearing in connection with said reading.

C. H. HARTKE,

recalled on behalf of the Plaintiff in rebuttal, further testified as follows:—

DIRECT EXAMINATION.

I recall the occasion of certain certificates of stock of the California Cotton & Factorage Company being issued in the name of J. B. SEARS, some 496 shares in all, but I don't remember the exact occasion as to when it was done. I had a conversation with Mr. West in connection with that matter in my office. Mr. Sears was present. This conversation took place about the 1st. day of December, 1920.

Q. What was the conversation?

A. Mr. West and Mr. Sears, in substance, asked me what the records showed as to the latest date that the stock appeared in the name of Mr. West, that is, the 496 shares, and I told them that my recollection was that the last time that was referred to in the minutes was the time we applied for an increase of the Capital Stock, which was May 20, and I so informed them, that that was the last record showing that the



(Testimony of C. H. Hartke.)

stock was in the name of Mr. West. That was practically all of that conversation.

Subsequent to that conversation I know that certificates for 496 shares of stock were issued in the name of J. B. SEARS. I can't say exactly as to when those certificates were issued but it was sometime after December 1st., 1920. The witness identified the 6 stock certificates 12 to 17 inclusive, the originals under stipulation to be forwarded to Clerk of Circuit Court of Appeals and stated that on each of the certificates save one is the witnesses signature. I put my signature as Secretary on those certificates along about December 1st., 1920. I was not Secretary of the Company at that time.

Q. BY THE COURT: Do you mean you put your signature on there as Secretary at that time when you were not Secretary?

A. Yes. May I explain the circumstances?

A. In the first place I was made Secretary for the purpose of letting Mr. Sears go back, and not as an officer, to prevent service being had on him by Shepard & Gluck—

That was the agreement between the Board, and that was the conclusion that they had come to, and they so decided, and—

A. (Continuing) Going back, then, it was sometime during the summer of 1920, I don't remember the exact date, the claim of Shepard & Gluck was being prosecuted and presented and we discussed informally—

(Testimony of C. H. Hartke.)

Q. Who is "we"?

A. The stockholders of the company,—the question of Mr. Sears going back to settle that claim.

MR. PARKE: May we find out who discussed this matter?

THE WITNESS: All the stockholders and directors.

A. (Continuing) And in the discussion that was had back and forth it was decided and said among them that I would be appointed Secretary—

A. (Continuing) I don't remember who said those different things; except that I was elected Secretary, and Sears didn't go back to Shepard & Gluck, and according to the records I remained Secretary until sometime in September. Then the question of the transfer of this stock came up and they told me that the transfer had been—

MR. PARKE: Now let us find out who told him.

A. (Continuing) Mr. West and Mr. Sears told me that they had transferred their stock and that it was done during the time that I was Secretary and for that reason I would have to sign the certificates as Secretary. They so told me, and although the transfer had not actually been made they explained that the arrangements had been made as of that time and they were dating it back.

#### CROSS EXAMINATION.

I observed that certain erasures had been made upon the certificates, that is there seems to have been a date filled in and then erased and a later date filled in. Mr.

(Testimony of C. H. Hartke.)

Norsworthy made the erasure, not in my presence but he acknowledged that he had done it along sometime after December 1st., 1920. He first had written December 1, or the numerals corresponding to that date in there. I did not see him write the date in there but I saw the figures in there before he had made the correction, and I recognized them as his handwriting.

Thereupon it was announced by counsel that there was no further rebuttal.

Counsel then requested permission of the court to present a request for special findings of fact, and it was stipulated by counsel, and consented to by the court, that the "request for special findings of fact" filed by the plaintiff and the defendant at the previous trial of this action before Judge Trippet, might be considered as re-filed as of this date and the request again made.

Whereupon defendant, through its attorney, made the following motion:

"In addition to the special findings of fact, if your Honor please, and before arguing the matter, if the Court desires to hear argument, the defendant, Maryland Casualty Company, desires to present a motion that the Court enter findings and judgment in favor of the defendant, and bases said motion upon the following grounds:

1. That the first cause of action as set forth in the original complaint as amended by the amendments thereto does not state facts sufficient to constitute a cause of action;



2. Upon the ground that the evidence is insufficient in that there is no evidence that the California Cotton & Factorage Company at any time became or was liable to the plaintiff bank in any sum for or on account of or by reason of the fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears while in the performance of his duties as secretary of the Cotton Company;

3. That the evidence is insufficient in that there is no evidence that said J. B. Sears converted to his own use or to the use of any other person, partnership or corporation, any of the money, property, rights or credits of the California Cotton & Factorage Company either through his fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication as set forth in plaintiff's first cause of action sued upon herein;

4. For the reason that the evidence is insufficient in that there is no evidence that J. B. Sears converted to his own use or to the use of any other person, partnership or corporation, other than the California Cotton & Factorage Company, any of the money, properties, rights, or credits of the California Cotton & Factorage Company, either through his fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication as set forth in plaintiff's second cause of action;

5. That the evidence is insufficient in that there is no evidence legally sufficient to show that the California Cotton & Factorage Company sustained any loss by



reason of any of the acts of said J. B. Sears through his fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication while in the performance of his duties as Secretary;

6. That the evidence is insufficient, towit, in that there is no evidence to show the value of any security or securities alleged to have been converted, embezzled, misappropriated or wilfully misapplied by J. B. Sears while in the performance of his duties as Secretary of the Cotton Company;

7. That the evidence is wholly insufficient, towit, in that there is no evidence that the Cotton Company sustained any loss by reason of any act or acts of fraud, embezzlement, misappropriation or misapplication alleged or proven to have been performed by J. B. Sears while acting within the scope of his authority as Secretary of the Cotton Company, the evidence showing that the losses, if any were sustained by the California Cotton & Factorage Company, were not sustained by reason of any act or acts of J. B. Sears, and if said losses were sustained they were sustained by acts of J. B. Sears in the performance of his duties as general manager, not secretary, of the California Cotton & Factorage Company, and are not covered by the bond sued upon herein;

8. That the evidence shows that the California Cotton & Factorage Company at all times knew of all the acts being performed by J. B. Sears and all of the acts alleged to have been performed by him, if performed, and consented to the continuance of such acts and did

not at any time prior to the 19th day of May, 1921, give notice to the defendant bonding Company of said act or acts so performed;

9. For the further reason that the evidence shows that the California Cotton & Factorage Company did not, within ten days after it became aware of the act or acts alleged to have occasioned the losses complained of, if any, notify the defendant Maryland Casualty Company of such act or acts or of the losses resulting therefrom as required under the policy of insurance and the application which is made a part thereof;

10. For the reason that the evidence shows that the California Cotton & Factorage Company failed to have its books, accounts, stocks and securities inspected, audited and verified with funds on hand or in bank each month by T. J. West, Treasurer of the Cotton Company, or failed to have its books, accounts, stocks and securities inspected and audited and verified with funds on hand or in bank and checked up each month by any person or persons as required under the bond and application made in connection therewith and which constitutes a part of the bond.

11. That the evidence shows that during all of the period of time during which the act or acts alleged and contended to have been performed by J. B. Sears and which it is claimed resulted in a loss, if any, sustained by the Cotton Company were performed by J. B. Sears, if at all, while he was the owner of 497 shares of the capital stock of the Cotton Company, and that during all of said time there were outstanding only

three additional shares: one each in the name of J. B. Conduit, T. W. McDevitt and C. H. Hartke, all of which certificates, while made out, had not been issued and delivered to said J. B. Conduit, T. W. McDevitt and C. H. Hartke; that each and all of said last mentioned parties paid no consideration for the stock so made out in their names and had no financial interest in the Company during said period of time, or in said corporation, and were dummy directors and officers, and the said California Cotton & Factorage Company as a corporation continued on and after May 24, 1920, and during the whole period of time during which acts complained of, if any, were performed by J. B. Sears; and during said period of time the said J. B. Sears was doing business through the corporation California Cotton & Factorage Company.

12. There is no evidence to support the allegations of plaintiff's complaint as amended.

That, I take it, is all, now, unless the Court desires the various matters argued.

THE COURT: Of course that motion indicates the reasons why you consider the judgment should be in your favor, and naturally would be considered with the whole case.

MR. PARKE: Yes, I understand that.

THE COURT: No particular ruling is now made on the motion.

MR. PARKE: No, I understand that."

It is stipulated that counsel for plaintiff at this time filed with the clerk and presented to the Court its spe-



cial findings of fact upon each and every of the issues of fact raised by the pleadings in the case, and at that time requested the Court to make its special findings in conformity with said special findings, and to sign special findings then submitted.

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL BANK	)	
OF LOS ANGELES,	)	
	)	REQUEST FOR
Plaintiff,	)	
vs.	:	SPECIAL FIND-
	)	
MARYLAND CASUALTY	)	INGS OF FACT
COMPANY, a corporation,	)	
	)	
Defendant.	)	

Comes now the Maryland Casualty Company, defendant herein, and respectfully requests the Court to make the following Special Findings of Fact herein:

I.

That the California Cotton & Factorage Company (hereinafter designated as Cotton Company) was organized on or about the 1st day of September, 1919, for the purpose of carrying on general brokerage business in the buying and selling of cotton and cotton products. That on or about the 8th day of September, 1919, the Cotton Company made written application to the plaintiff Bank for a line of credit not ex-



ceeding Two Hundred Thousand Dollars (\$200,000.00); that the plaintiff Bank granted said line of credit under the following Resolution by its Board of Directors passed on the 11th day of September, 1919, to-wit:

“Upon motion of G. W. Walker, seconded by A. J. Waters, and carried, a line of credit up to the maximum amount of \$200,000.00 at any one time was granted to the California Cotton & Factorage Company, the same to be guaranteed by its officers and secured by warehouse receipts for cotton, drafts with bill of lading attached for cotton, or advances to growers on crop mortgage or cotton.”

That in said written application for line of credit the Cotton Company stated and represented to the plaintiff Bank that in the purchase of cotton it would cause drafts to be drawn with warehouse or yard tickets attached covering the cotton purchased, same to be drawn by the seller upon the Cotton Company and after being accepted by the Cotton Company and guaranteed by its officers would be presented to the plaintiff Bank for payment for and on behalf of the Cotton Company; that for the more convenient handling and sale of the cotton so purchased, the plaintiff Bank would surrender and deliver up to the Cotton Company the warehouse or yard tickets attached to said drafts so accepted and accept in lieu thereof trust receipts in words and figures as follows, to-wit:

TRUST RECEIPT. NO.....

California Cotton & Factorage Co., Los Angeles, Cal.

Received in trust from the Citizens National Bank of Los Angeles, Bank of Los Angeles, documents described below, the purpose being to secure delivery of the shipments and secure outbound documents therefor which shall be returned to said Bank in cancellation of this receipt.

B/L No..... No. B. C..... Mark.....

CALIFORNIA COTTON & FACTORAGE CO.

J. B. SEARS, Mgr.

Compress or yard receipts

.....B/C attached.

That plaintiff Bank, relying upon the written application for line of credit so made to it, did thereafter and between September 8, 1919, and April 29, 1921, pay for and on behalf of the Cotton Company drafts which were drawn upon the Cotton Company and accepted by it and guaranteed by its officers in large numbers and in total sum aggregating not less than \$. . . . . ; that said Bank did also, pursuant to the written application so made, cause or permit each and all of the warehouse receipts or yard tickets attached to said drafts to be surrendered to the Cotton Company and accepted in lieu thereof trust receipts substantially in form as hereinbefore stated. That all said trust receipts were signed in the name of the Cotton Company by "J. B. Sears, Manager". That at the time the plaintiff Bank surrendered the warehouse receipts or yard tickets and accepted trust receipts it knew the cotton covered thereby would be by the Cot-

ton Company sold and disposed of in its regular course of business.

## II.

That thereafter and prior to April 29, 1921, all of the said drafts so paid and held by the plaintiff Bank were by the Cotton Company paid, save and except 87 drafts aggregating the principal sum of \$82,489.96, which drafts with trust receipts attached thereto plaintiff Bank now holds.

## III.

That the plaintiff Bank now holds trust receipts covering 1,476 yard tickets, each representing one bale of cotton. That 385 of said yard tickets have been returned to said Bank. That the cotton covered by the balance of said yard tickets was by the Cotton Company sold and disposed of in its regular course of business, and the total proceeds from the sale thereof deposited in the Cotton Company's general checking account in the plaintiff Bank, said deposits being represented by drafts drawn upon the purchaser, together with bill of lading covering the cotton so sold.

## IV.

That the Cotton Company paid and discharged all of the drafts held by plaintiff Bank, save and except 87, and secured release of the trust receipts attached thereto by check drawn in favor of the plaintiff Bank upon the Cotton Company's general checking account in plaintiff Bank. That throughout all the course of dealings between the plaintiff Bank and the Cotton Company, during the period from September 8, 1919, to April 29, 1921, the plaintiff Bank did not require



the "outbound documents" covering the cotton specified or covered by the trust receipts to be delivered back to the plaintiff Bank for the express purpose of cancelling the trust receipt held by plaintiff Bank but permitted the Cotton Company to deposit the "outbound documents" as a cash deposit in the Cotton Company's general checking account and permitted the Cotton Company to make payment of the drafts and secure release of the trust receipts held by the plaintiff Bank by check drawn upon the Cotton Company's checking account. That all of the drafts that were paid to the plaintiff Bank by the Cotton Company were paid in that manner.

V.

That the plaintiff Bank knew of and consented to the use by the Cotton Company of the moneys deposited in its general checking account in the payment of its general operating expenses and for other purposes than the payment to plaintiff Bank of the acceptances held by it.

VI.

That the plaintiff Bank, under the arrangements had with the Cotton Company at the time the \$200,000.00 maximum line of credit was extended, reserved to itself as additional security for any credit so extended, a lien upon all moneys on deposit at any time in the name of the Cotton Company in the Cotton Company's general checking account in plaintiff Bank.

VII.

That all of the cotton covered by the yard tickets surrendered to the Cotton Company by the Bank,



including those for which the plaintiff Bank now holds trust receipts, was by the Cotton Company sold and the total proceeds from the sale thereof deposited in the general checking account of the Cotton Company in plaintiff Bank. That all of the sums withdrawn from the plaintiff Bank were withdrawn by checks of the Cotton Company signed by its agent or officer having authority to sign checks and used by the Cotton Company in the general operation of its business and in payment of acceptances of plaintiff Bank.

#### VIII.

That the Cotton Company sustained no loss whatsoever by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication of moneys, securities or other personal property by J. B. Sears while in the performance of his duties as Secretary in the service of the Cotton Company.

#### IX.

That the loss sustained by the Cotton Company evidenced in part by its indebtedness to the plaintiff Bank was incurred not by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears while in the performance of his duties as Secretary in the service of the Cotton Company, but said loss accrued as a result of the purchase and sale of cotton in the regular course of the Company's business upon a declining cotton market.

X.

That said J. B. Sears did not at any time convert to his own use or to the use of any person or persons other than the Cotton Company any of the securities or other personal property referred to and described in plaintiff's first cause of action, or the proceeds thereof.

XI.

That J. B. Sears did not embezzle, wrongfully abstract or wilfully misapply any moneys, securities or other personal property belonging to the Cotton Company did not convert to his own use or to the use of any person or persons other than the Cotton Company any of the sum or sums set forth in plaintiff's second cause of action.

XII.

That books were kept by the Cotton Company in which were entered the description of all cotton received and sold and the cost and sale price thereof; all receipts and disbursements by the Cotton Company of its funds; all indebtednesses contracted with plaintiff Bank and all other financial transactions had by the Cotton Company. That said books so kept fairly and truly reflect the actual financial operations and conditions of the Cotton Company. That said books were kept by J. F. Norsworthy, employed by the Cotton Company as bookkeeper. That J. B. Sears did not cause said books to be kept in a false manner.

XIII.

That the Cotton Company was at all times aware of and had full knowledge of the operations of the Cotton Company by J. B. Sears as Secretary and/or

Manager and particularly its transactions with the plaintiff Bank. That J. W. McDevitt and T. J. West, as officers of the Cotton Company, knew of the arrangement made by the Cotton Company with the plaintiff Bank as to the manner in which the Cotton Company did business with said Bank, and knew that the Cotton Company was securing warehouse receipts or yard tickets from the bank and issuing trust receipts in lieu thereof, and that the cotton represented thereby was being sold and disposed of by the Cotton Company, and said J. W. McDevitt and T. J. West, as officers of said plaintiff Bank, consented thereto.

#### XIV.

That the issued capital stock of the Cotton Company was 500 shares of the par value of \$100.00 each. That on and after the 24th day of May, 1920, J. B. Sears was the owner and holder of 497 shares of said stock.

#### XV.

That J. B. Sears was Secretary of the Cotton Company from the date of its organization until May, 1920, at which time his written resignation was accepted by the Company and thereupon C. H. Hartke was elected Secretary; that the said C. H. Hartke held the office of Secretary until September 9, 1920, when his written resignation was accepted and J. B. Sears was re-elected to the office of Secretary and continued to hold the same until his death on May 3, 1921.

#### XVI.

That at all times from September, 1919, up to May 3, 1921, J. B. Sears was also General Manager of the Cotton Company and as such General Manager was,



by virtue of the By-laws of the corporation, vested with the entire charge and control of the Cotton Company's business.

XVII.

That at all times from the incorporation of the Cotton Company until May 24, 1920, T. J. West was Treasurer of the corporation. That no audit of the books of the Cotton Company was made at any time by T. J. West.

XVIII.

That the Cotton Company's books, accounts, stocks and securities were not inspected and audited nor were same verified with funds on hand or in bank at any time during the period covered by the bond sued upon herein by T. J. West nor by any other person during the period covered by the bond sued upon herein.

XIX.

That the Cotton Company knew at all times during the period covered by the bond sued upon herein that J. B. Sears, as General Manager, in the conduct of the Cotton Company's business, was withdrawing from the plaintiff Bank moneys deposited in said Bank to the credit of the Cotton Company and was using the money so withdrawn for the purpose of purchasing cotton and paying the operating expenses of the Cotton Company. That the Cotton Company also at all times knew that the money received by the Cotton Company from the sale of cotton covered by trust receipts held by the plaintiff Bank was being deposited to the checking account of the Cotton Company in plaintiff Bank



and was being withdrawn and used in payment for cotton purchased and in payment for the general operating expenses of the Cotton Company.

XX.

That the Cotton Company at all times during the period covered by the bond sued upon herein knew of the commission by said J. B. Sears, of the acts complained of and charged in plaintiff's Complaint as the basis for recovery against the defendant. That the Cotton Company permitted said J. B. Sears to continue the commission of such act or acts and did not at any time prior to the 19th day of May, 1921, notify the defendant Company thereof.

XXI.

That the Cotton Company did, prior to the 30th day of April, 1921, become aware of and knew of the commission by J. B. Sears of all the acts complained of and set forth in plaintiff's Complaint, but said Cotton Company did not, within ten days after becoming aware of the commission of said act or acts complained of, notify the defendant Company as required by the bond sued upon herein.

XXII.

That if any loss was sustained by the Cotton Company by reason of any act or acts of fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears while in the performance of his duties as Secretary and which occurred during the continuance of the bond sued upon, such loss was discovered by and known to the Cotton

Company prior to the 29th day of April, 1921, and notice of such loss

Thereafter, and after opinion of the Court had been rendered herein, application was made to the Court by plaintiff for permission to reconsider the date fixed by the Court when T. J. West sold and transferred his stock in the Cotton Company to J. B. Sears. Pursuant to said application the Court gave further consideration to said question, and thereafter, the parties hereto thereupon entered into the following stipulation:

“IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA SOUTHERN  
DIVISION

THE CITIZENS NATIONAL	(	
BANK OF LOS ANGELES,	)	
	(	No. 1124 Civil
Plaintiff,	)	
	(	
-vs-	)	STIPULATION
	(	
MARYLAND CASUALTY	)	
COMPANY,	(	
Defendant.	)	

The defendant herein having made application to the court for permission to re-open the case and introduce the testimony of Milton M. Carlson, a handwriting expert, as to the results of his examination of the stock register book of the California Cotton &

Factorage Company, and said application having been granted; NOW THEREFORE,

IT IS HEREBY STIPULATED between plaintiff and defendant, through their respective attorneys, as follows:

I.

That Milton M. Carlson is a handwriting expert and duly qualified as such to testify in relation to the subject matter hereinafter set forth.

II.

That said witness shall be deemed to have been sworn as a witness in the case and to have testified in accordance with letter bearing date January 9th, 1925, written to Messrs. Bicksler, Smith & Parke, attorneys at law, and signed by said Milton M. Carlson, which said letter is as follows:

‘MILTON CARLSON

Examiner & Photographer

Questioned Documents

306 International Bank Bldg.

Los Angeles

Los Angeles, January 9, 1925

Messrs. Bicksler, Smith & Parke,

Attorneys at Law,

829 Citizens National Bank,

Los Angeles, California

Attention Mr. Parke

Dear Sirs,—

At your request I have on January 8th and 9th, 1925, examined the stock certificate book of the California Cotton & Factorage Company, being one of the

exhibits on file in case U. S. 1124 Civil, Citizens National Bank -vs- Maryland Casualty Company, the said book being Defendant's Exhibit "B", and particularly stubs of stock certificates 12, 13, 14, 15, 16. These stock certificate stubs cover 400 shares of stock, issued in the name of J. E. Sears. The date of original issuance of these shares appears to have been erased on each of the aforementioned stubs, and the date "May 24, 1920" written over said erasure.

I have carefully examined the erasures to ascertain the date of issuance as originally written in said stubs and I find as follows:

THAT the original date written on the stubs, 12, 13, 14, 15, 16 was as follows—

"11/17 1920"

THAT the said date had been erased and obliterated in part, leaving however a sufficient form of figures to clearly determine that the original date of aforesaid stubs was:—

"11/17 1920".

Respectfully submitted,

MILTON CARLSON

MC:MQ

It is further stipulated that the original stock certificates numbers 12, 13, 14, 15 and 16, and 17, being certificates of stock of the California Cotton & Factorage Company, in the name of J. E. Sears, may be deemed to have been introduced and received in evidence.

Hunsaker, Britt & Cosgrove

Attorneys for Plaintiff

Blackler, Smith & Parks

Attorneys for Defendant."



For purposes of this Bill of Exceptions and in order that the Court of Appeals may have before it for inspection the stock certificate book and the original certificates of stock issued to J. B. Sears, said stock certificate book being Defendant's Exhibit "B", and said original stock certificates being the originals of which Exhibit "C" are copies, it is hereby stipulated and agreed that said original stock certificate book and said six (6) original certificates, being stock certificates numbers 12, 13, 14, 15 and 16, of the California Cotton & Factorage Company standing in the name of J. B. Sears, may be by the Clerk of the above entitled Court forwarded to and filed with the Clerk of the District Court of Appeals of the Ninth District, from which Court it is proposed to secure a Writ of Error herein.

Thereupon and after the Court had rendered its decision and judgment herein, upon stipulation the Court duly made and entered an Order giving the defendant to and including the 15th day of April, 1925, within which to prepare, serve and file its Bill of Exceptions herein, and thereafter and before the 15th day of April, 1925, upon further stipulation of counsel, the Court duly made and entered a further Order extending and enlarging to May 15, 1925, the time within which the defendant might serve and file its Bill of Exceptions; and thereafter and prior to the 15th day of May, 1925, the said Court, upon stipulation of counsel, extended and enlarged the time until June 15, 1925, within which defendant might prepare, serve and file its Bill of Exceptions herein, and said Bill of Ex-

ceptions has been prepared, served and filed within the time allowed by law and extended by stipulations of counsel and the Order of the Court, and counsel for defendant asks that the same be allowed and approved as correct.

And be it further remembered that the above and foregoing Bill of Exceptions is a full, true and correct statement of all of the evidence in the cause, and also of all objections, rulings and exceptions relied on by the defendant, and other proceedings in and upon the said trial; that no other different evidence, objections, rulings or exceptions relied on by said defendant or other proceedings were had in or upon said trial. And now, within due and proper time, said defendant, Maryland Casualty Company, a corporation, presents and introduces this, its said Bill of Exceptions, to said Court, and in order that said Exceptions may be preserved and perpetrated and in furtherance of justice and that right may be done, the said defendant, Maryland Casualty Company, presents the foregoing as its Bill of Exceptions herein and prays that the same may be settled, approved and allowed as true and correct in all particulars, and signed and *and* certified as provided by law and made a part of the records in the above entitled case.

Dated: 8th day of June, 1925.

MARLAND CASUALTY COMPANY,  
a corporation,

Defendant

By Bicksler Smith & Parke

Its Attorneys

STIPULATION APPROVING BILL OF  
EXCEPTIONS

It is hereby stipulated and agreed that the foregoing Bill of Exceptions is true and correct in all particulars, and that the same may be made a part of the records in the above entitled cause.

Dated: Los Angeles, California, this.....day of June, 1925.

CITIZENS NATIONAL BANK,  
a corporation,

Plaintiff,

By.....

Its Attorneys

MARLAND CASUALTY COMPANY,  
a corporation

Defendant,

By.....

Its Attorneys

Thereupon on Monday, July 27, 1925, pursuant to written notice served and filed on July 24, 1925 the matter of the settlement and signing of the foregoing bill of exceptions as amended came on regularly to be heard before the Honorable William P. James, sitting in chambers; and in support of said motion to settle said bill of exceptions as amended there was served and filed the following affidavit:

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL BANK )	
OF LOS ANGELES, )	
	) No. 1124—Civil.
Plaintiff, )	
	) AFFIDAVIT IN
vs. )	SUPPORT OF
	) "SETTLEMENT
MARYLAND CASUALTY )	AND ALLOW-
COMPANY, )	ANCE OF BILL
	) OF EXCEP-
Defendant (	TIONS."

COUNTY OF LOS ANGELES )	
	) SS.
STATE OF CALIFORNIA )	

DALE H. PARKE,

being duly sworn, deposes and says:

That he is a member of the copartnership of Bicksler, Smith & Parke, attorneys for the defendant herein.

That on the 14th. day of March, 1925, and within ten (10) days after the entry of judgment herein, affiant secured and filed stipulation and order of court extending the time within which defendant might prepare, serve, and file its bill of exceptions to the 15th. day of April, 1925; that on the 14th. day of April, 1925, affiant secured and filed in this court, order and stipulation extending defendant's time to prepare, serve and file its Bill of Exceptions to May 15th., 1925; that on May 15th, 1925, your affiant secured and filed in this



court stipulation and order extending defendant's time to prepare, serve and file its bill of exceptions to the 15th. day of June, 1925. That on the 10th. day of June, 1925, defendant's proposed bill of exceptions was prepared, served and filed. That thereafter, to-wit, on the 9th. day of June, 1925, stipulation was entered into between counsel for plaintiff and defendant as follows:—

“IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	
a corporation,	)	
	)	
Plaintiff,	)	
vs.	)	No. 1124 - Civil.
	)	
MARYLAND CASUALTY	)	
COMPANY, a corporation.	)	
Defendant.)	)	

STIPULATION EXTENDING TIME TO PRE-  
PARE PROPOSED AMENDMENTS TO  
PROPOSED BILL OF EXCEPTIONS OF  
MARYLAND CASUALTY COMPANY, A  
CORPORATION.

It is hereby stipulated by and between the parties hereto and their respective counsel that The Citizens National Bank of Los Angeles, a corporation, may have to and including July 9, 1925, within which to prepare and serve proposed amendments to the proposed bill

of exceptions of the Maryland Casualty Company, a corporation.

It is further agreed that this stipulation may, but need not be filed of record.

Dated June 9, 1925.

(Signed) HUNSAKER, BRITT & COSGROVE.

Attorneys for Plaintiff.

(Signed) BICKSLER, SMITH & PARKE.

Attorneys for Defendant."

That on the 8th. day of July, 1925, plaintiff, through its counsel, served and filed "Proposed Amendments to the Bill of Exceptions", which said proposed amendments contain fifty-nine (59) pages and contain Two Hundred Ninety-six (296) proposed amendments. That on receipt of the proposed amendments and upon checking same affiant found that a great many proposed amendments seemed to be without merit and thereupon your affiant called T. B. Cosgrove, one of the attorneys for plaintiff, by telephone and suggested that a great many of the proposed amendments seemed to be without merit, and suggested that a conference be had concerning the same. That at said telephone conversation said T. B. Cosgrove stated to affiant, "That the proposed amendments were prepared by two young men in our office during my absence and they may have been over cautious, and I suggest that you check the proposed amendments, indicating those you think are proper and those you think ought not to be allowed and return your copy of the proposed amendments with your notations thereon and I will check them over

within the next few days and let you know which ones we will insist upon." That pursuant to said request affiant checked all of the proposed amendments, making notations thereon of those approved by affiant and those not approved, and did on the 15th. day of July, 1925, return the copy of the proposed amendments so served upon attorneys for defendant with the notations thereon, and accompanied same by a letter as follows:—

"July 15, 1925.

Messrs. Hunsaker, Britt & Cosgrove,  
Attorneys-at-Law,  
Suite 1031 Title Insurance Bldg.,  
Los Angeles, Calif.

In re: Citizens Natl. Bank vs.  
Maryland Casualty Company.

Dear Mr. Cosgrove:

We are handing you our copy of your proposed amendments in Maryland Casualty Company case.

We have indicated with an "O. K." those we approve of, and by the word "No" those we think are sufficiently set forth in the Bill of Exceptions.

The notation "No" does not indicate that your proposed amendment is not supported by the transcript, but in most instances because we think the proposed Bill narrates the fact without setting forth so much detail

We believe the Bill of Exceptions should narrate as briefly as possible the ultimate facts as testified to by the witnesses, avoiding as much detail of testimony as possible.

We observe that objections are made to all exhibits upon the theory that copies attached are not true copies. The copies of all exhibits, except those which were set forth in the reporter's transcript were prepared by the Court Reporter and he assures us they are true copies. We personally have not compared them.

After checking over the proposed amendments in view of the foregoing, and the notations thereon, the writer will be pleased to go over the proposals in detail so that the proposed bill may be rewritten, if possible, during the week.

Very truly yours,

DHP/W

BICKSLER, SMITH & PARKE."

Encl.

That thereafter, and between July 15th., 1925, and July 22nd., 1925, affiant called Mr. T. B. Cosgrove on two occasions, asking how soon he would complete his re-checking of the proposed amendments and was advised by him that the re-checking would be made within a day or two. That during the afternoon of July 22nd., 1925, the said T. B. Cosgrove returned to affiant the proposed amendments with certain notations made thereon and which did not appear upon the "Proposed Amendments" when first served, and said T. B. Cosgrove accompanied said return with a letter as follows:—



"July 22nd., 1925.

IN RE CITIZENS NATIONAL BANK V MARY-  
LAND CASUALTY CO.

Messrs. Bicksler, Smith & Parke,  
Citizens National Bank Bld.,  
Los Angeles, Calif.

ATTENTION MR. PARKE.

Gentlemen:

Responding to your esteemed favor of the 15th. instant in the above entitled matter, we wish at the outset to express our opinion that the time for settling a bill of exceptions in the above entitled matter has expired; that the court is without jurisdiction to settle a bill of exceptions at this time, and that the same may not legally be incorporated into a printed transcript of record upon writ of error.

If we err in the matter just stated, and a judge of the local District Court undertakes to settle your proposed bill of exceptions, we shall, with regard to our proposed amendments, take the position as reflected by the following references:

Subdiv. I. Our proposed amendments numbered respectively 3, 5, 11, 17, 29, 30, 31, 34, 47, 49, 54, 55, 56, 70, 92, 98, 99, 120, 129, 140, 141, 142, 143, 145, 146, 147, 148, 171, 175 if 168 is denied, 176, 191, 192, 193, 194, 195, 197, 199, 200, 201, 202, 204, 208, 209, 215, 219, 250, 251, 252, 253, 257, 258, 259, 260, 265, 277, 286 and 287 will not be insisted upon.

Subdiv. II. Exhibit number 2, pages 2, 3, and 4 of the proposed bill is marked Exhibit number 1. Exhibit

number 1, pages 5, 6, 7 and 8 of the proposed bill is marked exhibit number 2.

(1) Accordingly, these exhibits should be correctly numbered.

(2) The answer to question number 12, page 7, (proposed transcript, plaintiff's exhibit 1, incorrectly marked exhibit number 2), must be corrected to correspond with original. We attach importance to the printed portion of the answer omitted in your proposed bill.

(3) The trust receipt as copied into the proposed bill, pages 19 and 20, is difficult to understand, and because of the importance of the document, we suggest that the instrument be copied as originally printed, and as the same appears in page 7 of plaintiff's complaint,

(4) On page 31 of the proposed bill of exceptions, is an incorrect copy of plaintiff's exhibit 11. When re-copying this instrument do not omit time and place where the same originated, as shown upon the original.

(5) On pages 12 and 13 of the proposed bill are extracts from the bylaws of the Cotton Company. If you do not wish to print the entire set of bylaws then in addition to article 3, we wish to have inserted article 4, relating to certificates of stock and transfers. We suggest also on page 12, line 4, the elimination of the words "were read in evidence" and the substitution therefor of the word "are" In lines 10 and 11 the insertion of section 2---, and section 3---, and elimination of the statement "that is section 1, section 4 reads". Also the elimination on page 12, line 29, of the following sentence: "This is the important portion of it."

(6) The original exhibit number 5 copied into your proposed bill, pages 13, 14 and 15, was upon the letterhead of the Cotton Company. When page 13 is rewritten we wish the printed matter appearing on the letterhead to appear. There are typographical errors at line 10 and 13, page 15.

(7) The letter dated August 9, 1921, being part of plaintiff's exhibit 13, appearing on page 47 of your proposed bill does not bear the signature "G. F. Cushwa." The original marked as an exhibit bears this signature.

(8) On page 157½ reference is made to defendant's exhibit F, and a portion of one of the exhibits is thereafter copied into the proposed bill. Immediately following the end of page 160 we wish inserted either this notation "Other portions of said exhibit consisting of cancelled checks and sheets containing pencilled memoranda are not copied into this bill of exceptions," or copies of the checks and pencilled memoranda, as you prefer.

(9) Our proposed amendment number 246 is not correctly stated. Line 23 which now reads "246. P. 155, l. 16, after the word: "books", strike out" should read "246. P. 155, l. 19, after the word: "acceptance" strike out".

It may appear that some of the suggestions in this subdivision may refer to proposed amendments mentioned in the first subdivision. If so, the waiver of the amendment as proposed is conditioned upon the adoption of the suggestion herein contained.



Subdiv. III. Proposed amendments not approved by you and marked O. K. upon your copy of the proposed amendments, and not heretofore in subdivision I or subdivision II referred to, will be insisted upon.

For your accommodation we will hold ourselves in readiness to confer with you personally, or appear upon written notice at any time during the ensuing week or thereafter, before Judge James, to discuss the matter of the settlement of the proposed bill.

With sincere feelings of esteem, we are,

Very truly yours,

HUNSAKER, BRITT & COSGROVE

TBC:A (Signed) By T. B. COSGROVE."

That affiant received said letter upon his return to the office at 5.30 P. M. on July 22nd., 1925.

That on the morning of July 23rd., 1925, Mr. T. B. Cosgrove called affiant by telephone and suggested that he would be pleased to confer with us regarding possible settlement of the proposed amendments which had not theretofore been approved by us, and to that end affiant and said T. B. Cosgrove devoted substantially the entire day of July 23rd., 1925, and a portion of July 24th., 1925, to a rechecking of the proposed amendments. That an agreement was had for the waiving of approximately sixty (60) of plaintiff's proposed amendments in addition to those waived in the letter aforementioned.

That at the time the original bill of exceptions was served upon plaintiff's counsel, to-wit, on June 9th., 1925, request was made of plaintiff's counsel to indi-



cate what portions of certain exhibits the plaintiff desired copied into the record. The exhibits referred to were the two auditor's reports and the minutes and by-laws of the corporation. At that date counsel for plaintiff stated that he would advise counsel for defendant as to the portions of said exhibits the plaintiff would desire copied into the bill of exceptions. That plaintiff did not until the 25th. day of July, 1925, indicate what portions of defendant's Exhibit E (Farrar's report); Exhibit 14 (Cole's report); and Exhibit A (Minutes of the Cotton Company) he desired printed in the bill of exceptions. That on July 25th., 1925, affiant received a letter from plaintiff's counsel, the original of which is hereto attached and made a part of this affidavit.

There was not sufficient time intervening between July 8th, 1925, the date on which plaintiff's "Proposed Amendments" were served and July 12th 1925 the end of the term of court, within which said amendments might have been made by reason of the great number of amendments proposed. That affiant has devoted practically his entire time since July 22nd., 1925, the date on which plaintiff returned its corrected copy of proposed amendments in arriving at an agreement with counsel for plaintiff as to proposed amendments and the making of said amendments. That agreement between counsel as to the amendments to be waived was not had until Saturday, July 25th., 1925, when counsel for plaintiff delivered their letter of July 25th., 1925, attached hereto.

That the making of the agreed corrections in said bill required the re-writing of a large portion thereof and to that end a public stenographer was employed on Friday, July 25th., 1925., who worked thereon continuously during working hours and same was not completed until the morning of July 27th., 1925.

That of the amendments originally proposed by plaintiff aggregating 296, approximately 121 were later, by agreement of plaintiff's counsel, waived.

Further affiant saith not.

Dale H Parke

Subscribed and sworn to before me this 27 day of July, 1925.

Myrtle M. Reeder

Notary Public in and for the County of Los Angeles, State of California.

(Seal)

Thereupon said Citizens National Bank of Los Angeles by counsel filed its written objection to the settlement of said proposed bill of exceptions and objected to the settlement of said proposed bill of exceptions upon the grounds and for the reasons that the term of the Court at which the action was tried, the findings signed, and the decision entered had expired; that the time allowed for settling and signing said bill of exceptions had expired; that no order of the Court, nor of any judge thereof, had been made and entered, nor had the consent of the plaintiff and defendant in error, or any of its attorneys, been given. extending the time within which to settle and sign said bill of excep-

tions beyond the term in which said action was tried and said judgment signed and entered; that no very extraordinary circumstances have been shown to justify the Court in entertaining the application to settle and sign said bill of exceptions at this time; and that no motion for new trial, or any other motion or proceeding in said action was pending and undisposed of upon the termination of said term in which said action was tried. And thereafter in support of said objection filed the following affidavit:

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124 - Civil
	)	
Plaintiff,	)	
	)	AFFIDAVIT IN
VS.	)	SUPPORT OF
	)	OBJECTION TO
MARYLAND CASUALTY	)	SETTLEMENT OF
COMPANY,	)	PROPOSED BILL
Defendant.	)	OF EXCEPTIONS.
	)	

STATE OF CALIFORNIA,           )  
                                                  ) SS.  
COUNTY OF LOS ANGELES. )

T. B. COSGROVE,

being first duly sworn, upon oath deposes and says:

That he is an attorney at law and a member of the law firm of Hunsaker, Britt & Cosgrove, attorneys for

the plaintiff herein; that judgment in the above entitled action was entered on March 9, 1925; that on June 10, 1925, defendant served upon counsel for plaintiff and lodged with the Clerk of the court its proposed bill of exceptions, consisting of 188 pages; that thereafter on July 9th plaintiff served upon counsel for defendant and lodged with the clerk of the court its proposed amendments to the proposed bill of exceptions containing 296 proposed amendments; that on Wednesday, July 15th, 1925, affiant received from counsel for defendant a letter reading as follows, being accompanied with a copy of proposed amendments theretofore served upon them:

"July 15, 1925.

Messrs. Hunsaker, Britt & Cosgrove,  
Attorneys-at-law,  
Suite 1031 Title Insurance Bldg.,  
Los Angeles, Calif.

In re: Citizens Natl. Bank vs.  
Maryland Casualty Company.

Dear Mr. Cosgrove:

We are handing you our copy of your proposed amendments in Maryland Casualty Company case.

We have indicated with an "O. K." those we approve of, and by the word "No" those we think are sufficiently set forth in the Bill of Exceptions.

The notation "No" does not indicate that your proposed amendment is not supported by the transcript, but in most instances because we think the proposed Bill narrates the fact without setting forth so much detail.



We believe the Bill of Exceptions should narrate as briefly as possible the ultimate facts as testified to by the witnesses, avoiding as much detail of testimony as possible.

We observe that objections are made to all exhibits upon the theory that copies attached are not true copies. The copies of all exhibits, except those which were set forth in the reporter's transcript were prepared by the Court Reporter and he assures us they are true copies. We personally have not compared them.

After checking over the proposed amendments in view of the foregoing, and the notations thereon, the writer will be pleased to go over the proposals in detail so that the proposed bill may be rewritten, if possible, during the week.

Very truly yours,  
BICKSLER, SMITH & PARKE,  
DALE H. PARKE.

DHP/W  
Encl."

That thereafter on July 22, 1925, affiant delivered the following communication to counsel for defendant:

“July 22nd, 1925.

IN RE CITIZENS NATIONAL BANK V  
MARYLAND CASUALTY CO.

Messrs. Bicksler, Smith & Parke,  
Citizens National Bank Bldg.,  
Los Angeles, Cal.

ATTENTION MR. PARKE

Gentlemen:

Responding to your esteemed favor of the 15th instant in the above entitled matter, we wish at the outset to express our opinion that the time for settling a bill of exceptions in the above entitled matter has expired; that the court is without jurisdiction to settle a bill of exceptions at this time, and that the same may not legally be incorporated into a printed transcript of record upon writ of error.

If we err in the matter just stated, and a judge of the local District Court undertakes to settle your proposed bill of exceptions, we shall, with regard to our proposed amendments, take the position as reflected by the following references:

Subdiv. I. Our proposed amendments numbered respectively 3, 5, 11, 17, 29, 30, 31, 34, 47, 49, 54, 55, 56, 70, 92, 98, 99, 120, 129, 140, 141, 142, 143, 145, 146, 147, 148, 171, 175 if 168 is denied, 176, 191, 192, 193, 194, 195, 197, 199, 200, 201, 202, 204, 208, 209, 215, 219, 250, 251, 252, 253, 257, 258, 259, 260, 265, 277, 286 and 287 will not be insisted upon.

Subdiv II. Exhibit number 2, pages 2, 3, and 4 of the proposed bill is marked Exhibit number 1. Ex-

hibit number 1, pages 5, 6, 7 and 8 of the proposed bill is marked exhibit number 2.

(1) Accordingly, these exhibits should be correctly numbered.

(2) The answer to question number 12, page 7, (proposed transcript, plaintiff's exhibit 1, incorrectly marked exhibit number 2), must be corrected to correspond with original. We attach importance to the printed portion of the answer omitted in your proposed bill.

(3) The trust receipt as copied into the proposed bill, pages 19 and 20, is difficult to understand, and because of the importance of the document, we suggest that the instrument be copied as originally printed, and as the same appears in page 7 of plaintiff's complaint.

(4) On page 31 of the proposed bill of exceptions, is an incorrect copy of plaintiff's exhibit 11. When re-copying this instrument do not omit time and place where the same originated, as shown upon the original.

(5) On pages 12 and 13 of the proposed bill are extracts from the bylaws of the Cotton Company. If you do not wish to print the entire set of bylaws then in addition to article 3, we wish to have inserted article 4, relating to certificates of stock and transfers. We suggest also on page 12, line 4, the elimination of the words "were read in evidence" and the substitution therefor of the word "are." In lines 10 and 11 the insertion of section 2 \* \* \*, and section 3 \* \* \*, and elimination of the statement "that is section 1,

section 4 reads". Also the elimination on page 12, line 29, of the following sentence: "This is the important portion of it."

(6) The original exhibit number 5 copied into your proposed bill, pages 13, 14 and 15, was upon the letterhead of the Cotton Company. When page 13 is rewritten we wish the printed matter appearing on the letterhead to appear. There are typographical errors at lines 10 and 13, page 15.

(7) The letter dated August 9, 1921, being part of plaintiff's exhibit 13, appearing on page 47 of your proposed bill does not bear the signature "G. F. Cushwa." The original marked as an exhibit bears this signature.

(8) On page 157½ reference is made to defendant's exhibit F, and a portion of one of the exhibits is thereafter copied into the proposed bill. Immediately following the end of page 160 we wish inserted either this notation "Other portions of said exhibit consisting of cancelled checks and sheets containing pencilled memoranda are not copied into this bill of exceptions," or copies of the checks and pencilled memoranda, as you prefer.

(9) Our proposed amendment number 246 is not correctly stated. Line 23 which now reads (246. P. 155, l. 16, after the word: "books", strike out" should read "246. P. 155, l. 19, after the word: "acceptance" strike out".

It may appear that some of the suggestions in this subdivision may refer to proposed amendments men-



tioned in the first subdivision. If so, the waiver of the amendment as proposed is conditioned upon the adoption of the suggestion herein contained.

Subdiv. III. Proposed amendments not approved by you and marked O. K. upon your copy of the proposed amendments, and not heretofore in subdivision I or subdivision II referred to, will be insisted upon.

For your accommodation we will hold ourselves in readiness to confer with you personally, or appear upon written notice at any time during the ensuing week or thereafter, before Judge James, to discuss the matter of the settlement of the proposed bill.

With sincere feelings of esteem, we are

Very truly yours,

HUNSAKER, BRITT & COSGROVE,

By T. B. COSGROVE.

TBC:A"

That on July 24, 1925, affiant received from counsel for defendants communication reading as follows:

"July 24th, 1925.

Messrs. Hunsaker, Britt & Cosgrove,

Attorneys-at-law,

Title Insurance Building,

Los Angeles, Calif.

Attention: Mr. Cosgrove.

Dear Mr. Cosgrove:

We are handing you herewith copy of the testimony of Mr. C. H. Hartke which you desire included in the Bill of Exceptions.

We hope the draft as prepared will meet with your approval. If not, will you kindly telephone the writer.

We are also serving herewith Notice of Presentation of Bill of Exceptions. You will note therein that we dissent to certain of the amendments as proposed by you. We desire to give you the notice at this time although we hope that before Tuesday morning all matters between us will be agreed on.

We are having prepared the portion of the "Minutes" and of the "By-laws" as requested by you, and are also having copies made of certain of the additional exhibits as agreed upon.

Very truly yours,  
BICKSLER, SMITH & PARKE,  
By DALE H. PARKE.

DHP/W  
Encl."

That on July 25, 1925, affiant delivered to counsel for defendant a communication reading as follows:

"July 25th, 1925.

IN RE CITIZENS NATIONAL BANK V.  
MARYLAND CASUALTY CO.

Messrs. Bicksler, Smith & Parke,  
Citizens National Bank Bldg.,  
Los Angeles, Cal.

ATTENTION MR. PARKE

Gentlemen:

In response to oral request of your Mr. Parke so to do, and supplementing our communication to you of the 22nd instant, we desire:

First, to reiterate our opinion that the time for settlement of bill of exceptions in the above entitled matter has expired, and that the Court is without jurisdiction to settle the proposed bill. To the end, however, that you may be in a position to submit your proposed bill for settlement, and have the question passed upon by the Court, we make the following suggestions:

Second, (a) In the place of copying into the proposed bill plaintiff's entire exhibit number 14, as specified in our proposed amendment number 53, copy only such portions of said exhibit as appear upon the first and the last, and the last but one pages of the report of July 15, 1921, the same being one of the two reports constituting said exhibit number 14.

(b) In the place of copying into the proposed bill defendants entire exhibit "E", as specified in our proposed amendment number 229, substitute the following stipulation:

"It is stipulated that between the 19th day of November, 1920, and the 25th day of April, 1921, eighty-seven (87) sight drafts were accepted by J. B. Sears, and that said eighty-seven (87) acceptances are in the total amount of Eighty-two thousand, four hundred eighty-seven 96/100 (\$82,487.96) dollars. That between said 19th day of November, 1920, and the 1st day of December, 1920, twenty-five (25) of said eighty-seven (87) sight drafts were accepted by J. B. Sears, and that said twenty-five (25) acceptances are in the total amount of Twenty-nine thousand, three

hundred thirty-seven 99/100 (\$29,337.99) dollars. That attached to said eighty-seven (87) sight drafts were fourteen hundred seventy-six (1476) warehouse receipts for fourteen hundred seventy-six (1476) bales of cotton, and that attached to said twenty-five (25) sight drafts were four hundred fifty-five (455) warehouse receipts for four hundred fifty-five (455) bales of cotton. That between said 19th day of November, 1920, and said 25th day of April, 1921, plaintiff delivered to said J. B. Sears said fourteen hundred seventy-six (1476) warehouse receipts, and accepted therefor eighty-seven (87) trust receipts, and between said 19th day of November, 1920, and said 1st day of December, 1920, plaintiff delivered to said J. B. Sears said four hundred fifty-five (455) warehouse receipts and accepted therefor twenty-five (25) trust receipts. That upon the death of said J. B. Sears said California Cotton & Factorage Company had in its possession and thereafter surrendered to said Citizens National Bank three hundred eighty-five (385) of said fourteen hundred seventy-six (1476) warehouse receipts. That seventy-six (76) of said three hundred eighty-five (385) warehouse receipts so surrendered were originally attached to said twenty-five (25) sight drafts accepted by said J. B. Sears between said 19th day of November, 1920, and said first day of December, 1920, and that said seventy-six (76) warehouse receipts had been delivered to said J. B. Sears by said Citizens National Bank between said 19th day of November, 1920, and said 1st day of December, 1920. That said four hundred fifty-five (455) bales



of cotton cost said California Cotton & Factorage Company at the time of its purchase, and was then of the value of Twenty-nine thousand, three hundred thirty-seven 99/100 (\$29,337.99) dollars. That said three hundred eighty-five (385) bales of cotton at the time of its purchase cost said California Cotton & Factorage Company, and was then of the value of Twenty-one thousand, eight hundred ninety-three 34/100 (\$21,893.34) dollars. That said seventy-six (76) bales of cotton at the time of its purchase cost said California Cotton & Factorage Company, and was then of the value of Five thousand, fifty-six 02/100 (\$5,056.02) dollars.

That upon the death of said J. B. Sears, said California Cotton & Factorage Company did not have in its possession and did not thereafter surrender to said Citizens National Bank ten hundred ninety-one (1091) of said fourteen hundred seventy-six (1476) warehouse receipts. That said ten hundred ninety-one (1091) bales of cotton represented thereby cost said California Cotton & Factorage Company at the time of its purchase, and was then of the value of Sixty thousand, five hundred ninety-four 62/100 (\$60,594.62.)”

(c) In the place of copying into the proposed bill defendant's entire exhibit number “A”, as specified in our proposed amendment number 190, copy only such portions of said exhibit as appear in the minutes of the special meetings of the Board of Directors, held May 20, 1920, and September 9, 1920, respectively, including also a stipulation to the effect that

between said dates there were no regular or special meetings held by the stockholders or directors of the California Cotton & Factorage Company.

(d) You may consider that our proposed amendment number 291 suggesting an incorporation into the proposed bill of plaintiff's request for special findings of fact is waived, but in lieu thereof insert a stipulation indicating that the plaintiff at that time did file and request the court, etc.

(e) Our proposed amendment number 290, testimony of C. H. Hartke—in the draft of testimony of C. H. Hartke accompanying your letter to us of the 24th instant, the following corrections should be made in order to conform with the transcript:

(1) Page 1, lines 26 and 27, strike out "being plaintiff's exhibit . . ., and stated that the signatures on each of the certificates," and substitute therefor "(the originals under stipulation to be forwarded to Clerk of Circuit Court of Appeals) and stated that the signature on each of the certificates save one."

(2) Page 2, line 0, before line 1 insert the following: "Yes, may I explain the circumstance."

(3) Page 2, line 14, after the word "stockholders" insert "and directors."

(4) Page 3, line 4, strike out the words "some other", and insert "a later".

In our opinion the necessity for this last correction amply justifies the care given in this office to the examination of the proposed bill.

Your notice of presentation of bill served upon us yesterday contains this unusual declaration: "The

final draft of your proposed amendments to the proposed bill of exceptions heretofore filed by the defendant was received July 22, 1925." Such declaration, as you well know, has no place in a form of notice. Moreover, although it may represent your contention or opinion, it does not state the fact: the fact being that the document you refer to as having been received on July 22, 1925, is a letter from this office notifying you of the expiration of the time within which to settle the bill, and further declaring that if we are mistaken in this connection, and the Court proceeds to a settlement of the proposed bill, the particulars in which we would waive, and those in which we would insist upon, our proposed amendments, heretofore on July 9, 1925, served upon you and lodged with the Clerk of the Court. To the end that no misunderstandings as to statements may later arise, we have notified the Official Court Reporter that his presence is desired on Monday next, July 27, 1925, when you present your proposed bill for settlement. We will at that time also request that the matter be taken up in open Court.

Enclosed herewith, pursuant to your request, we are handing you our copy of the report of R. W. E. Cole, of date July 15th, 1921; and being a part of plaintiff's exhibit number 14, referred to in our proposed amendment number 53.

Very respectfully yours,  
HUNSAKER, BRITT & COSGROVE,  
By T. B. COSGROVE

encl.

TBC:A"

That on July 27, 1925, affiant received from counsel for defendant a communication reading as follows:

“July 27, 1925.

Messrs. Hunsaker, Britt & Cosgrove,  
Attorneys-at-law,  
Title Insurance Company,  
Los Angeles, Calif.  
Attention Mr. T. B. Cosgrove.

In re: Citizens National Bank vs.  
Maryland Casualty Company.

Gentlemen:

We are handing you herewith original “Bill of Exceptions as Amended”. All amendments proposed by you, and not heretofore by agreement waived, have been made in the original Bill, except that there is no copy of Exhibit 19. This is the exhibit which is missing from the court files. Mr. Ross Reynolds, Court Reporter, who receipted for the exhibit advises that he can find no trace thereof.

A number of pages of the bill of exceptions as originally proposed have been re-written, while a number of pages have been corrected by interlineation.

As per your request, we are handing you copies of the re-written pages. Attached to the re-written pages are notations indicating by number the amendment to which they relate.

In order to enable you to check the amendments which have been interlineated on the original pages of the bill as filed, we are handing you the original bill of exceptions as amended, with the request that you return the same to us in good time so that we



may present same to the Court tomorrow morning for settlement.

Kindly acknowledge receipt of the proposed bill as amended for the purposes aforesaid, indicating also what, if any, stipulation or order of court you desire made as regards the lost Exhibit No. 19.

Very truly yours,

BICKSLER, SMITH & PARKE,  
BY DALE H. PARKE.

Received original "Bill of Exceptions as Amended"  
as per above letter, this 27th day of July, 1925.

.....

Attorneys for Plaintiff."

That said proposed amended bill of exceptions consisted of 257 pages. That no stipulation either oral or written was made or entered into between counsel for the respective parties extending the time for the settlement of a bill of exceptions beyond the expiration of the term in which judgment was entered, and that subsequent to the expiration of said term no stipulation either oral or written has been made or entered into between counsel for the respective parties providing that the Court may settle a bill of exceptions after the expiration of said term; that no order of the Court nor of any judge thereof has been made extending the time within which said bill of exceptions may be settled and signed, beyond said term, and that no motion or proceeding in said action was pending and undisposed of upon the termination of said term in which said action was tried and said judgment en-

tered; that counsel for defendant has never requested  
affiant, nor any member of said firm of Hunsaker,  
Britt & Cosgrove, for a stipulation extending the time  
within which to settle and have signed a bill of excep-  
tions beyond said time.

Further affiant saith not.

T. B. Cosgrove

SUBSCRIBED AND SWORN TO before me this  
29th day of July, 1925.

Lloyd E. Keiser (Seal)

Notary Public for County of Los Angeles,  
State of California.

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL BANK )  
 OF LOS ANGELES, ) No. 1125-Civil.  
 COMPANY, a corporation, )  
 Plaintiff, ) ORDER SET-  
 ) TLING BILL  
 vs. ) OF EXCEP-  
 ) TIONS.  
 MARYLAND CASUALTY )  
 )  
 Defendant. )

Defendant has presented its bill of exceptions, together with amendments thereto offered by the plaintiff and accepted by the said defendant, for settlement. The plaintiff, by its counsel, has objected to settle.

ment being made of the bill, for the reason that the term within which the judgment was entered has expired and no order of court has been made nor stipulation entered into extending the time beyond the end of the term for the purpose of settling the bill. The term has expired and no order of court was made extending the time to cover the date of presentation and it is claimed that no stipulation was made answering to the same purpose. In connection with the preparation of this bill the following facts appear:

That the time within which defendant could serve and file its bill of exceptions was by stipulation of counsel and order of court enlarged and extended to June 15th, 1925; that defendant served and filed its bill of exceptions on June 10th, 1925; that by stipulation and consent of counsel for plaintiff and defendant the time within which plaintiff might propose amendments to the bill of exceptions was enlarged and extended to and including July 9th, 1925; that on July 8th, 1925, plaintiff served its proposed amendments and same were filed on July 9th, 1925; that said proposed amendments contained two hundred and ninety-six (296) amendments; that thereafter, to-wit, on July 22nd, 1925, additional and further amendments to said bill of exceptions were proposed by plaintiff. That between the said 9th day of July, 1925, and the date of this order negotiations toward an agreement between counsel, covering the proposed amendments, were pending and said proposed amendments were not finally agreed upon between the parties until the 25th day of July, 1925, and said bill of exceptions as

amended was upon notice presented on this date for allowance and settlement; that while counsel for the plaintiff did proceed to discuss the matter of the substance of the bill and his amendments thereto after the term had expired, he did inform counsel for the defendant in writing that he did not waive the objection that the bill was not presented in time, and advised said counsel that he would insist upon said objection.

That by reason of the facts the Court considers that good cause exists for the settlement of said bill of exceptions on this date. The objection of the plaintiff to the settlement of the bill is overruled and an exception is allowed to the plaintiff.

IT IS HEREBY ORDERED that said bill of exceptions as amended be, and the same is hereby, settled, allowed and approved as true and correct in all particulars; and it is hereby further ordered by said court that said bill of exceptions be, and the same is hereby, made a part of the record in the above-entitled cause.

Given, made and dated at Los Angeles, California, this 29th day of July, 1925.

WM P JAMES

District Judge.

(Endorsed): No. 1124-Civil. U. S. DISTRICT COURT, SOUTHERN DISTRICT OF CALIFORNIA, SOUTHERN DIVISION. CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, a corporation, Defendant. ORDER SETTLING BILL OF EXCEPTIONS. FILED JUL 29 1925 CHAS. N. WILLIAMS, Clerk by Murray E. Wire, Deputy Clerk.



IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	:	No. 1124-Civil.
	)	
Plaintiff,	:	
	)	SUPPLEMENTAL
vs.	:	ORDER TO ORDER
	)	SETTLING BILL OF
MARYLAND CASUALTY	:	EXCEPTIONS.
COMPANY, a corporation,	)	
	:	
Defendant.)	)	
	:	

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It appearing that, through inadvertence, the following words and statement were inserted in the order settling bill of exceptions as filed on July 29, 1925:

“that thereafter, to-wit, on July 22nd, 1925, additional and further amendments to said bill of exceptions were proposed by plaintiff.”

IT IS NOW ORDERED that said order be amended and that such words and statement as aforesaid be stricken from said order.

Dated this 30th day of July, 1925.

Wm P JAMES

District Judge.

[Endorsed]: No. 1124-Civil. U. S. DISTRICT COURT SOUTHERN DISTRICT OF CALIFORNIA SOUTHERN DIVISION. CITIZENS NA-

TIONAL BANK OF LOS ANGELES, vs. MARYLAND CASUALTY COMPANY, a corporation. SUPPLEMENTAL ORDER TO ORDER SETTLING BILL OF EXCEPTIONS. FILED Jul 30 1925 CHAS. N. WILLIAMS, Clerk Murray E. Wire Deputy

[Endorsed]: No 1124 Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California Southern Division In the matter of Citizens National Bank of Los Angeles a corp Plf vs Maryland Casualty Co. a corp Deft Proposed Bill of Exceptions This Copy of Proposed Bill of Exceptions served upon us this 27th day of July 1925 Hunsaker Britt & Cosgrove attorneys for Citizens National Bank of Los Angeles Lodged JUN 10 1925 CHAS. N. WILLIAMS, Clerk By L. J. Cordes Deputy Clerk Engrossed Bill of Exceptions FILED JUL 31 1925 CHAS. N. WILLIAMS, Clerk By R S. Zimmerman Deputy Clerk Bicksler, Smith & Parke 829 Citizens National Bank Bldg. Fifth and Spring Sts. Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Plf

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL	)	No. 1124--Civil.
BANK,	)	
	)	
Plaintiff,	)	
	)	STIPULATION
-vs-	)	EXTENDING
	)	TIME TO
MARYLAND CASUALTY	)	PREPARE BILL
COMPANY,	)	OF EXCEPTIONS
	)	
Defendant.	)	

IT IS HEREBY STIPULATED by and between the parties herein that defendant may have until and including April 15th, 1925, within which to prepare, serve and file its bill of exceptions herein.

Dated—March 12th, 1925.

BICKSLER, SMITH & PARKE,  
Attorneys for Defendant.

Hunsaker, Britt & Cosgrove  
Attorneys for Plaintiff.

It is so ordered.

Dated—March 13, 1925.

Wm P. James

Judge of the U. S. District Court.

[Endorsed]: (ORIGINAL) No. 1124-Civil IN  
THE UNITED STATES DISTRICT COURT In  
and for the Southern District of California, SOUTH-  
ERN DIVISION In the Matter of THE CITIZENS

NATIONAL BANK, Plaintiff, -vs- MARYLAND CASUALTY COMPANY, Defendant. STIPULATION EXTENDING TIME TO PREPARE BILL OF EXCEPTIONS FILED MAR 13 1925 CHAS. N. WILLIAMS, Clerk By L J Cordes Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts., Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Defendant.

IN THE DISTRICT COURT OF THE UNITED STATES SOUTHERN DISTRICT OF CALIFORNIA SOUTHERN DIVISION

THE CITIZENS NATIONAL)	No. 1124 - Civil
BANK,	)
Plaintiff,	)
	)
-vs-	)
	)
MARYLAND CASUALTY )	STIPULATION
COMPANY,	)
	)
	)
Defendant.	)

IT IS HEREBY STIPULATED by and between the parties herein that defendant may have until and including the 15th day of May, 1925, within which to prepare, serve and file its bill of exceptions herein.

Dated April 13th, 1925.

BICKSLER, SMITH & PARKE  
Attorneys for Defendant  
Hunsaker Britt & Cosgrove  
Attorneys for Plaintiff

It is so ordered.

Dated April 14, 1925.

Wm P James  
Judge of the U. S. District Court



[Endorsed]: No. 1124 Civ. In The UNITED STATES DISTRICT COURT In and for the Southern District of California, SOUTHERN DIVISION THE CITIZENS NATIONAL BANK, -VS- MARYLAND CASUALTY COMPANY, No. 1124-Civil STIPULATION EXTENDING TIME TO PREPARE BILL OF EXCEPTIONS FILED APR. 14 1925 CHAS. N. WILLIAMS, Clerk By Edmund L. Smith Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts., Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Defendant

IN THE DISTRICT COURT OF THE UNITED  
STATES SOUTHERN DISTRICT OF  
CALIFORNIA SOUTHERN  
DIVISION

THE CITIZENS NATIONAL)	No. 1124 - Civil
BANK,	)
Plaintiff,	)
	)
-vs-	) STIPULATION
	) EXTENDING
	) TIME TO
MARYLAND CASUALTY )	PREPARE BILL
COMPANY,	) OF EXCEPTIONS
	)
Defendant.	)

IT IS HEREBY STIPULATED by and between the parties herein that defendant may have until and

including the 15th day of June, 1925, within which to prepare, serve and file its bill of exceptions herein.

Dated April 14, 1925.

BICKSLER, SMITH & PARKE  
Attorneys for Defendant  
Hunsaker Britt & Cosgrove  
Attorneys for Plaintiff

It is so ordered.

Dated May 15 1925.

Wm P James

Judge of the United States District Court

[Endorsed]: No. 1124-Civil In The UNITED STATES DISTRICT COURT In and for the Southern District of California, Southern Division THE CITIZENS NATIONAL BANK, VS MARYLAND CASUALTY COMPANY STIPULATION EXTENDING TIME TO PREPARE BILL OF EXCEPTIONS FILED MAY 15 1925 CHAS. N. WILLIAMS, Clerk By Edmund L. Smith Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts., Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Defendant

IN THE DISTRICT COURT OF THE UNITED  
STATES FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL  
BANK, OF LOS ANGELES,  
a corporation,

Plaintiff,

vs.

MARYLAND CASUALTY  
COMPANY, a corporation,

Defendant.

No. 1124-Civil.

STIPULATION EXTENDING TIME TO PRE-  
PARE PROPOSED AMENDMENTS TO PRO-  
POSED BILL OF EXCEPTIONS OF MARY-  
LAND CASUALTY COMPANY, A CORPO-  
RATION.

It is hereby stipulated by and between the parties hereto and their respective counsel that The Citizens National Bank of Los Angeles, a corporation, may have to and including July 9, 1925, within which to prepare and serve proposed amendments to the proposed bill of exceptions of the Maryland Casualty Company, a corporation.

It is further agreed that this stipulation may, but need not be filed of record.

Dated June 9, 1925.

Hunsaker Britt & Cosgrove  
Attorneys for Plaintiff.  
Bicksler Smith & Parke  
Attorneys for Defendant.

[Endorsed]: COPY No. 1124 - Civil IN THE UNITED STATES DISTRICT COURT Southern District of California Southern Division THE CITIZENS NATIONAL BANK, OF LOS ANGELES, a corporation, Plaintiff, vs. MARYLAND CASUALTY COMPANY, a corporation, Defendant. STIPULATION EXTENDING TIME TO PREPARE PROPOSED AMENDMENTS TO BILL OF EXCEPTIONS OF MARYLAND CASUALTY COMPANY, A CORPORATION. FILED JUL 28 1925 CHAS. N. WILLIAMS, Clerk By R. S. Zimmerman Deputy Clerk. HUNSAKER, BRITT & COSGROVE 1031-1044 Title Insurance Building Fifth and Spring Streets LOS ANGELES, CAL. Attorneys for Plaintiff.

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION.

CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124 - Civil
	)	
Plaintiff,	)	NOTICE OF
	)	PRESENTATION
vs.	)	OF BILL OF
	)	EXCEPTIONS FOR
MARYLAND CASUALTY	)	ACCEPTANCE.
COMPANY,	)	
	)	
Defendant.	)	

To the plaintiff, and to HUNSAKER, BRITT & COSGROVE, its Attorneys:



The final draft of your proposed amendments to the proposed Bill of Exceptions, heretofore filed by the defendant, was received July 22nd., 1925.

NOTICE IS HEREBY GIVEN, that the defendant dissents to certain of the amendments as proposed by you.

NOTICE IS FURTHER GIVEN, that on Tuesday, the 28th. day of July, 1925, at the hour of 9.30 o'clock A. M., the defendant will present to WILLIAM P. JAMES, Judge of the above-entitled Court the proposed Bill of Exceptions for settlement and allowance.

DATED: July 24th., 1925.

Bicksler Smith & Parke

Attorneys for Defendant.

[Endorsed]: No. 1124—Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California, Southern Division CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, Defendant NOTICE OF PRESENTATION OF BILL OF EXCEPTIONS FOR ACCEPTANCE. Received copy of the within notice this 24 day of July 1925. Filed Jul. 28-1925 CHAS. N. WILLIAMS, Clerk, By R. S. ZIMMERMAN, Deputy Clerk Hunsaker, Britt & Cosgrove attorney for Plf BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth & Spring Sts. Los Angeles, Cal. Telephone TRINITY 4331 Attorneys for Defendant.

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124—Civil
	)	
Plaintiff,	)	
vs.	)	PETITION
	)	FOR WRIT OF
MARYLAND CASUALTY	)	ERROR.
COMPANY, a Corporation,	)	
	)	
Defendant.	)	

The above-named defendant, MARYLAND CASUALTY COMPANY, a Corporation, conceiving itself aggrieved by the final judgment given, made and entered by the above-entitled court, in the above-entitled cause, upon the issues therein joined, under date of March 7th, A. D. 1925, said judgment being now on file in said cause and court, it hereby petitions the above-entitled court for an order allowing it to prosecute a writ of error to the United States Circuit Court of Appeals for the Ninth Circuit, at San Francisco, in the State of California, from said judgment, and from the whole thereof, for the reasons set forth in the assignments of errors, which is filed herewith, under and pursuant to the law of the United States in that behalf made and provided; and it prays that this petition for said writ of error may be allowed, and that a transcript of the record, proceedings and papers upon which said judgment was given, made and entered as aforesaid, duly authenticated, may be sent

to the United States Circuit Court of Appeals for the Ninth Circuit, at the City of San Francisco, in the State of California.

DATED: This 6th day of July, A. D. 1925.

Bicksler, Smith & Parke,  
Attorneys for Plaintiff in Error.

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IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124—Civil
	)	
Plaintiff	)	
vs	)	ASSIGNMENTS
	)	OF ERROR
MARYLAND CASUALTY	)	
COMPANY, a Corporation,	)	
	)	
Defendant.	)	

- - - - -

Now comes the above named defendant, plaintiff in error herein, and says that in the record and proceedings in the above entitled action there is manifest error, and now makes, presents and files the following assignments of error upon which it will rely, as follows, to-wit:

I

That the first cause of action as set forth in plaintiff's original complaint as amended by the amendments thereto does not state facts sufficient to con-

stitute a cause of action against the defendant herein and the Court erred in over-ruling defendant's demurrer thereto.

## II.

The Court erred in over-ruling defendant's motion for non-suit and defendant's motion that the Court enter findings and judgment in favor of the defendant.

## III

The evidence received upon the trial of the above entitled action was and is wholly insufficient to justify the findings of the trial Court that the California Cotton & Factorage Company sustained any loss of any kind or character by reason of any fraud, dishonesty, forgery, embezzlement, wrongful abstraction or wilful misapplication by J. B. Sears while in the performance of his duties as secretary of the said California Cotton & Factorage Company.

## IV.

The evidence received upon the trial of the above entitled action was and is wholly insufficient to justify the finding of the trial Court as set forth in finding of fact No. VI that the said J. B. Sears applied to and secured from the plaintiff the warehouse receipts

“with the intent then and there by him entertained of fraudulently and dishonestly converting, misappropriating, and wilfully misapplying said warehouse receipts, the cotton represented thereby, and any money or proceeds obtained therefrom, and with the further fraudulent and dishonest intent then and there by him entertained, of thereby causing a loss to said California Cotton &



Factorage Company of money, securities, and personal property for which it would be and has become responsible to the plaintiff herein”.

V.

There is no evidence to justify that part of the finding of the Court No. VI insofar as the Court finds that the said J. B. Sears at the time of executing the trust receipts and securing delivery to him of the warehouse receipts, or cotton tickets, made any other or different representations to the plaintiff or any of its officers than the representations set forth in the letter of September 8, 1919, written by the California Cotton & Factorage Company to the plaintiff bank, being plaintiff's Exhibit No. 5.

VI.

There is no evidence to justify that part of finding of fact of the Court No. VI wherein the Court found that

“and pursuant to said fraudulent and dishonest plan and scheme said J. B. Sears at various times and irregular intervals procured from the plaintiff herein between the 19th day of November, 1920 and said 25th. day of April, 1921, 1,476 warehouse receipts for 1,476 bales of cotton and issued and delivered to the plaintiff in acknowledgment thereof 87 of said trust receipts.”

for the reason that the evidence shows that the securing of said warehouse receipts for 1,476 bales of cotton and the issuance and delivery of the 87 trust receipts therefor was done and performed by said J. B.

Sears with the consent and knowledge of the plaintiff and pursuant to and in strict keeping with the plan of operations entered into and agreed upon by and between the plaintiff and the California Cotton & Factorage Company as evidenced by the letter of September 8, 1919, plaintiff's Exhibit No. 5.

VII.

There is no evidence to justify that part of finding of fact of the Court No. VII to the effect that said J. B. Sears

“without the knowledge of said California Cotton & Factorage Company, or any of its officers or agents other than J. B. Sears, pursuant to said fraudulent and dishonest plan and scheme by him entertained as hereinbefore found, fraudulently and dishonestly converted, misappropriated and wilfully misapplied 1,091 of said 1,476 warehouse receipts and 1,091 bales of cotton represented thereby.”

VIII.

There is no evidence to justify that part of finding of fact of the Court No. VII that said J. B. Sears in performing the acts as set forth in said finding No. VII violated any of his duties as secretary or violated any of the promises and representations made by him to the plaintiff or that in depositing outbound drafts covering cotton sold, he, the said J. B. Sears, made any misrepresentations to the officer or officers of the plaintiff bank or caused said sight drafts to be deposited as cash items in the account of the California Cotton & Factorage Company for the purpose of de-

frauding or cheating the plaintiff bank or of defrauding or cheating the plaintiff or said California Cotton & Factorage Company or of misapplying or misappropriating any of its property.

IX.

There is no evidence to support that part of the finding of fact of Court No. VII that the said J. B. Sears pursuant to said alleged fraudulent scheme or otherwise or at all falsified the books and accounts of the California Cotton & Factorage Company in the manner as set forth in finding of fact No. VII or otherwise or at all and particularly that he falsified the books and accounts of the said California Cotton & Factorage Company by entering or causing to be entered therein the various amounts of money received from the sales of cotton and carrying same upon the bank pass book as monies and funds belonging entirely without limitation of any kind to the said Company; or that he wilfully failed to enter in the books of said Company any entry or memorandum indicating that trust receipts had been issued to the plaintiff covering the cotton that was being sold and disposed of or that he wilfully failed to make or cause to be made any entry or memorandum indicating that the monies received from the sale of cotton was charged with any trust or were in any manner monies or funds other than the absolute and unencumbered funds of the said Cotton Company.

X.

There is no evidence to support that part of finding of fact of the Court No. VII that said J. B. Sears

frequently represented to the California Cotton & Factorage Company, its officers and directors, that the various sums of money and credits entered upon the bank pass book and books of account of the Cotton Company were the funds and monies of the said Cotton Company or to the effect that the plaintiff or said California Cotton & Factorage Company, or any of its officers and directors, relied upon or were deceived by any dishonest or false and fraudulent representations made to them by said J. B. Sears.

XI.

That there is no evidence to support or justify that part of finding of fact of the Court No. VII that the 1,091 bales of cotton sold and disposed of by the Cotton Company and for which the plaintiff held trust receipts was at the time the same was sold and disposed of, of the reasonable value of \$60,594.62 or any part thereof or any sum whatsoever.

XII.

There is no evidence to support or justify that portion of finding of fact of the Court No. VIII that said J. B. Sears did secure possession of the warehouse receipts held by plaintiff as collateral security by any false or fraudulent representations or that in selling and disposing of the cotton covered by trust receipts held by the plaintiff the said J. B. Sears acted in a fraudulent or dishonest manner or was guilty of any conversion, misappropriation or wilful misapplication of said warehouse receipts or of the cotton covered thereby, and that said J. B. Sears in selling



and disposing of said cotton or in disbursing the proceeds realized from the sale thereof was acting in a false or fraudulent manner or practicing any deceit upon the plaintiff or upon the California Cotton & Factorage Company,

### XIII.

There is no evidence to support or justify that part of finding of fact of the Court No. VIII that said J. B. Sears

“fraudulently and dishonestly converted, misappropriated and wilfully misapplied the monies and funds placed to the credit of the said California Cotton & Factorage Company following the dishonest and fraudulent sales of cotton and disposition of warehouse receipts and bills of lading, all as herein found, by using said monies and funds for the purpose of dealing and speculating in cotton in the name of the said California Cotton & Factorage Company and conducting such dealings and speculations at a loss and paying said losses out of said monies and funds and in the payment of claims and demands incurred by said J. B. Sears in said dealings and speculations in cotton.”

### XIV.

There is no evidence to support or justify that part of the finding of fact of the Court No. VIII that

“relying entirely upon said false and fraudulent representations of said J. B. Sears herein found and said deceits by him practiced upon it and

them as herein found, said California Cotton & Factorage Company, its directors and officers, continued the business of said California Cotton & Factorage Company and consented to said J. B. Sears, subsequent to said 19th. day of November, 1920, continuing to act as the secretary of said Company—and to continue to deal and speculate in cotton and to incur indebtedness and contract financial obligations in connection therewith as herein found.”

XV.

There is no evidence to justify or support that portion of finding of fact of the Court No. IX that the California Cotton & Factorage Company sustained any loss or has become responsible to the plaintiff herein in the sum of \$60,594.62, or any sum of money whatsoever, with interest thereon by reason of any fraud, dishonesty, wrongful abstraction and wilful misapplication of said 1,091 warehouse receipts, and/or the cotton held thereunder, and/or said bills of lading, and/or the money proceeds and credits realized from the sale thereon but on the contrary said evidence shows that said indebtedness existing in favor of the plaintiff against the California Cotton & Factorage Company was incurred pursuant to and in strict keeping with the plan of operations agreed upon between the plaintiff and the California Cotton & Factorage Company as evidenced by the letter of September 8, 1919, plaintiff's Exhibit No. 5, and that all of the monies received from the sale of the said 1,091 bales of cotton was received by and deposited in plaintiff

bank to the credit of the California Cotton & Factorage Company and no part of said cotton evidenced by said 1,091 warehouse receipts or any of the monies realized from the sale thereof was lost to the California Cotton & Factorage Company.

#### XVI.

That there is no evidence to support or justify any finding by the trial Court that the said J. B. Sears in securing the 1,476 warehouse receipts from the plaintiff and issuing and delivering to plaintiff in acknowledgment thereof 87 trust receipts or in selling and disposing of 1,091 bales of cotton evidenced by said warehouse receipts and covered by said trust receipts was acting pursuant to any fraudulent or dishonest intent or design on his part or in violation of any agreement or representations made by him or by the California Cotton & Factorage Company to the plaintiff in relation to said warehouse receipts and the cotton covered thereby. The evidence conclusively shows that the securing of said warehouse receipts and the issuance of trust receipts to the plaintiff was known to and approved of by the officers and directors of the plaintiff and of the California Cotton & Factorage Company.

#### XVII.

There is no evidence to support or justify any finding of the trial Court that said J. B. Sears in depositing the "outbound documents" covering the sale of cotton for which the plaintiff bank held trust receipts as a cash item to the credit of the California Cotton & Factorage Company was acting pursuant to any fraud-



ulent or dishonest intent or design on the part of the said J. B. Sears for the reason that on the contrary the evidence shows that the officers and directors of the plaintiff and of the California Cotton & Factorage Company knew and approved of the handling of the sale of said cotton and the disbursement of the funds realized thereupon in the manner in which the same were handled by said J. B. Sears.

XVIII.

There is no evidence to support or justify the finding of fact of the Court No. X that within ten days after the California Cotton & Factorage Company discovered the alleged loss claimed to have been sustained by it, it notified the defendant herein of said alleged loss and of the facts in connection therewith.

XIX.

There is no evidence to justify or support the finding of fact of the Court Nos. XIV and XV that J. B. Sears was not allowed and permitted by the California Cotton & Factorage Company as he deemed best.

XX.

There is no evidence to support or justify that part of the finding of fact of the Court No. XVI that T. J. West, treasurer of said California Cotton & Factorage Company,

“visited the office of the said California Cotton & Factorage Company semi-monthly during the term of said bond as herein found and at such times conferred with J. B. Sears respecting the business of said Company and checked over the



books of said Company but not in detail at any time. examining the cotton account, being the purchase and sales cotton account, showing the cotton bought and sold and at said times examined the records disclosing the amount of cotton bought, the amount of cotton sold, the number of bales unsold, the entries respecting the hedging of the same, and also examined the cash account and the acceptance account, together with the cotton tickets indicating the number of bales of cotton on hand and compared the same and determined that they corresponded to the acceptances in the plaintiff bank and that at such times said T. J. West checked the books of said Company for the purpose of determining the amount of money owing by said Company to said Citizens National Bank and examined the statements and books of said Company and did observe the amount of cotton purchased, the number of cotton tickets and bales of cotton on hand, and examined the ledger books of said Company and the various accounts therein including the cotton account, and checked the same with the bookkeeper's statement furnished at the end of each month.";

or that

"that said T. J. West checked the accounts of said Company, including the bank account, semi-monthly by said statements rendered by the bookkeeper as herein found"

or that

“that it is not true that if an audit had been made each month as provided in the contract between the California Cotton & Factorage Company and said defendant it would have revealed the facts as herein found and that the loss herein found to have been sustained could have been checked, lessened and stopped.”

XXI.

There is no evidence to support or justify that portion of finding of fact of the Court No. XVII that the California Cotton & Factorage Company or the plaintiff herein did not discover the alleged loss claimed to have been sustained by the California Cotton & Factorage Company by the alleged acts of J. B. Sears until the 19th. day of May, 1921.

XXII.

There is no evidence to justify or support the finding of fact of the Court No. XIX that it is not true that all of the monies of the California Cotton & Factorage Company handled by J. B. Sears were used in and for the purchase of cotton and other commodities for the Cotton Company or for the purpose of paying the expenses or costs of operation of the Cotton Company.

XXIII.

There is no evidence to support or justify that portion of finding of fact of the Court No. XIX that the warranties made by the California Cotton & Factorage Company to the defendant in the application for bond were not untrue or were not broken in all or any

of the respects as alleged in defendant's answer; or that the defendant is or has not been released from all or any of the obligations of liability to plaintiff under said bond sued upon herein; or that the California Cotton & Factorage Company has not breached any of the warranties of said bond or done anything contrary to or in violation of the terms of the application for said bond.

#### XXIV.

There is no evidence to support or justify the finding of fact of the Court No. XX that the alleged loss to the California Cotton & Factorage Company was not incurred with the full knowledge of the officers and directors of said Cotton Company and with their consent.

#### XXV.

There is no evidence to justify or support that portion of the finding of fact of the Court No. XXI that the sale and transfer by T. J. West of 496 shares of stock to said J. B. Sears occurred on the 1st. day of December, 1920, or at any date subsequent to the 17th day of November, 1920; or that it was only on and after December 1, 1920, that J. B. Sears became and was the practical owner of the entire assets and business of said Cotton Company.

#### XXVI.

There is no evidence to support or justify that part of the finding of fact of the Court No. XXIV that the 455 bales of cotton covered by sight drafts accepted by the plaintiff prior to December 1, 1921, were at

the time the same were disposed of by J. B. Sears had the reasonable value of \$29,337.99 or any part thereof or any sum whatsoever.

XXVII.

That the Court erred in its conclusions of law in finding that the plaintiff is entitled to judgment against the defendant on its first cause of action in the sum of \$24,321.97, together with interest thereon, or any sum whatsoever.

XXVIII.

That the Court erred in giving, making, rendering, and filing its judgment in the above-entitled action in favor of the plaintiff and against the defendant in this, that said final judgment was and is contrary to law and to the cause made and facts stated in the pleadings and records in said action.

XXIX.

That the Court erred in failing and refusing to make findings of fact herein in accordance with the "Request for Special Findings of Fact" as made by the defendant to the trial Court prior to the submission of said case for the Court's decision, and which "Request for Special Findings" is set forth in the Transcript of the Record herein.

XXX.

That the Court erred in failing to find as a fact that T. J. West sold and transferred to J. B. Sears 496 shares of the capital stock of the California Cotton & Factorage Company on or prior to the 17th. day of November, 1920, and that at all times on and after



November 17, 1920, said California Cotton & Factorage Company was a corporation sole, to-wit, J. B. Sears, and under his exclusive management and control.

### XXXI.

That the Court erred in failing to find as a fact that the said California Cotton & Factorage Company failed to do and perform those promises and warranties set forth in the application for bond made by said California Cotton & Factorage Company to defendant in that the said California Cotton & Factorage Company did not by and through its treasurer, T. J. West, cause the books and records of said California Cotton & Factorage Company to be inspected and audited and verified with funds on hand or in bank as expressly provided for in paragraph 12 of the application made by the said California Cotton & Factorage Company to the defendant for said bond.

In order that the foregoing Assignments of Error may appear of record said defendant presents the same to said Court and prays that such disposition be made thereof as is in accordance with law and the statutes of the United States in such cases made and provided; and said defendant, plaintiff in error herein, prays the reversal of the above mentioned final judgment heretofore given, made, rendered, entered and filed in the above entitled *Cout* in the above-entitled action.

Dated at Los Angeles, California, this 6th day of July 1925.

MARYLAND CASUALTY COMPANY,  
a corporation

Defendant and Plaintiff in Error.

By Bicksler, Smith & Parke

Its Attorneys.

UNITED STATES OF AMERICA )  
 ) SS.  
SOUTHERN DISTRICT OF CALIFORNIA )

We, the undersigned, attorneys for the above-named defendant, plaintiff in error herein, do hereby certify that the foregoing Assignments of Error is made on behalf of said defendant and is in our opinion well taken and the same now constitutes the Assignments of Error upon the writ prayed for.

Dated at Los Angeles, California, this 6 day of July 1925.

Bicksler, Smith & Parke

Attorneys for Defendant.

[Endorsed]: No. 1124—Civil In The UNITED STATES DISTRICT COURT In and for the Southern District of California, Southern Division THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY a corporation Defendant. PETITION FOR WRIT OF ERROR FILED JUL 6 1925 CHAS. N. WILLIAMS, Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts. Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Plaintiff in Error.

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124—Civil
	)	
Plaintiff,	)	
vs.	)	ORDER
	)	ALLOWING
MARYLAND CASUALTY	)	WRIT OF ERROR
COMPANY, a Corporation,	)	
	)	
Defendant.	)	

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At a stated term, to-wit, the January Term, 1925, of the above-entitled court, held at its court-room at the City of Los Angeles, in the State of California, on the 6th day of July, A. D. 1925.

Present: The Honorable WILLIAM P. JAMES, Judge of said Court.

Upon the petition of Maryland Casualty Company, a corporation, and on motion of its counsel:

It is hereby ordered that a writ of error to the United States Circuit Court of Appeals for the Ninth Circuit at the City and County of San Francisco, State of California, from the final judgment heretofore given, made, filed and entered in and by the above-named court, in the above-entitled cause, upon the issues therein joined, under date of March 9, 1925, be, and the same is hereby allowed; and that a certified transcript of the record, testimony, exhibits, stipu-

lations, bill of exceptions, and all proceedings herein, be forthweith transmitted to said United States Circuit Court of Appeals, for the Ninth Circuit. It is further ordered that upon the filing by the defendant and plaintiff in error of a good and sufficient bond on writ of error, approved by this Court, in the sum of Forty Thousand Dollars, all further proceedings in this court be suspended and stayed until the determination of said Writ of Error by the United States Circuit Court of Appeals for the Ninth Circuit.

Dated Los Angeles, California, this 6 day of July, 1925.

Wm P James.

Judge of said Court.

[Endorsed]: No. 1124—Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California, SOUTHERN DIVISION THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, a Corporation, Defendant. ORDER ALLOWING WRIT OF ERROR. FILED JUL 6 1925 CHAS. N. WILLIAMS, Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts. Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Defendant



IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	
	)	
	)	No. 1124—Civil
Plaintiff,	)	R E C E I P T
vs.	)	
MARYLAND CASUALTY	)	
COMPANY, a Corporation,	)	
	)	
Defendant.	)	

Received a copy of:—

ORDER ALLOWING WRIT OF ERROR,  
PETITION FOR WRIT OF ERROR,  
and  
ASSIGNMENTS OF ERROR,

in the above entitled matter this 6th. day of July, 1925.

Hunsaker, Britt & Cosgrove

Attorneys for Plaintiff.

[Endorsed]: No. 1124—Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California SOUTHERN DIVISION THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff, vs. MARYLAND CASUALTY COMPANY, a Corporation, DEFENDANT RECEIPT FOR COPY OF DEEDS FILED Jul 7 1925 CHAS. N. WILLIAMS, Clerk By L. J. Cordes Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth and Spring Sts. Los Angeles, Cal. Telephone TRinity 4331 Attorneys for Defendants.

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA, SOUTHERN  
DIVISION.

THE CITIZENS NATIONAL )	
BANK OF LOS ANGELES,) No. 1124-Civil	
Plaintiff, )	
vs. )	BOND
MARYLAND CASUALTY )	ON WRIT OF
COMPANY, a Corporation, )	ERROR.
Defendant. )	

KNOW ALL MEN BY THESE PRESENTS:

That we, MARYLAND CASUALTY COMPANY, a Corporation, as principal, and FIDELITY AND DEPOSIT COMPANY OF MARYLAND, as Surety, are held and firmly bound unto the defendant in error, The Citizens National Bank of Los Angeles, a Corporation, in the full and just sum of Forty Thousand (\$40,000.00) Dollars, to be paid to the said defendant in error, its attorneys, successors and assigns; to which payment well and truly to be made we bind ourselves, our heirs, executors, administrators, successors and assigns, jointly and severally by these presents. Sealed with our seals and dated this 16th day of July, 1925.

WHEREAS, lately in the above-entitled Court, in an action *depending* in said Court between the Citizens National Bank of Los Angeles, a corporation, as plaintiff, and Maryland Casualty Company, a Corporation, as defendant, a judgment was rendered against said defendant, and said defendant having obtained a writ of error and filed a copy thereof in the Clerk's

office of said Court, to reverse the judgment in the aforesaid suit, and a citation directed to said plaintiff, citing and admonishing it to be and appear at a session of the United States Circuit Court of Appeals, for the Ninth Circuit, to be holden in the City and County of San Francisco, State of California, in said Circuit, on the 4th day of August, A. D. 1925.

Now, the condition of the above obligation is such that if the said defendant shall prosecute said writ of error to effect and answer all damages and costs if it fail to make the said plea good, then the above obligation to be void; else, to remain in full force and virtue; and,

WHEREAS, the said defendant desires to stay the execution of said judgment so sought to be reversed, the said Fidelity and Deposit Company of Maryland does further, in consideration thereof and of the premises, undertake and promise and does acknowledge itself bound in the said sum of Forty Thousand (\$40,000.00) Dollars, being an amount in excess of said judgment, that if said judgment so sought to be reversed under said writ of error, or any part thereof, be affirmed, or said writ of error be dismissed, the said defendant, Maryland Casualty Company, a Corporation, will pay to The Citizens National Bank of Los Angeles, a Corporation, the amount directed to be paid by the said judgment, or the part of such amount as to which the same shall be affirmed, if affirmed only in part, and all damages and costs which may be awarded against the defendant upon the appeal, and

that if the said defendant does not make such payment within thirty (30) days after the filing of the mandate from the United States Circuit Court of Appeals in the Court to which said writ of error is issued, judgment may be entered in said action on motion of the plaintiff and without notice to the said Fidelity and Deposit Company of Maryland in favor of said plaintiff against the undersigned surety, for such amount, together with the interest that may be due thereon, and the damages and costs which may be awarded against the defendant upon said Writ of Error.

IN WITNESS WHEREOF, the said Fidelity and Deposit Company of Maryland has caused its name to be set, and its corporate seal to be affixed by its duly authorized officers at Los Angeles, California, this 16th day of July, 1925.

MARYLAND CASUALTY COMPANY,  
a Corporation

By E. F. Kreamer

Manager, Southern California  
Claim Division

FIDELITY AND DEPOSIT COMPANY  
OF MARYLAND

By W. M. Walker

Its Attorney-in-Fact

(Seal)

Attest

S. M. Smith

Agent



County of Los Angeles, )  
 State of California ) SS

On the 20th day of July, 1925, before me, W. C. Smith, a Notary Public in and for the County and State aforesaid personally appeared E. F. KRAEMER, known to me to be the person whose name is subscribed to the foregoing instrument as Manager of Maryland Casualty Company, a Corporation, and he acknowledged to me that said Maryland Casualty Company, a Corporation, executed the same.

W. C. Smith (Seal)

NOTARY PUBLIC

In and for the County of Los  
 Angeles, State of California.

STATE OF CALIFORNIA, )  
 ) ss  
 County of Los Angeles )

On this 16 day of July, 1925, before me T. E. Seaton, a Notary Public, in and for the County and State aforesaid, duly commissioned and sworn, personally appeared W. M. Walker and S. M. Smith known to me to be the persons whose names are subscribed to the foregoing instrument as the Attorney-in-Fact and Agent respectively of the Fidelity and Deposit Company of Maryland, and acknowledged to me that they subscribed the name of Fidelity and Deposit Company of Maryland thereto as Principal and their own names as Attorney-in-Fact and Agent, respectively.

(Seal)

T. E. Seaton

Notary Public in and for the State  
 of California, County of Los Angeles.

Examined and Recommended for approval as provided in Rule 28

Bicksler, Smith & Parke

Attorneys for Defendant.

The foregoing bond is hereby approved this 20 day of July, 1925.

Wm. P. James

Judge.

[Endorsed]: No. 1124-Civil In The UNITED STATES DISTRICT COURT In and for the Southern District of California Southern Division THE CITIZENS NATIONAL BANK OF LOS ANGELES, Plaintiff vs. MARYLAND CASUALTY COMPANY, a Corporation, Defendant. BOND ON WRIT OF ERROR FILED JUL 20 1925 CHAS. N. WILLIAMS, Clerk By R. S. Zimmerman Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth & Spring Sts. LOS ANGELES, CAL. Telephone TRinity 4331 Attorneys for Plaintiff in error.

IN THE DISTRICT COURT OF THE UNITED  
STATES, SOUTHERN DISTRICT OF  
CALIFORNIA, SOUTHERN  
DIVISION

CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124 - Civil
	)	
Plaintiff	)	AMENDED
vs.	)	PRAECIPE FOR
	)	TRANSCRIPT OF
MARYLAND CASUALTY	)	RECORD
COMPANY,	)	
Defendant	)	

TO THE CLERK OF THE ABOVE ENTITLED  
COURT:

You will please prepare transcript of record in the above entitled cause, to be filed in the office of the clerk of the United States Circuit Court of Appeals for the Ninth Judicial Circuit, under the writ of error heretofore issued out and perfected, to said court, and include in said transcript the following pleadings, proceedings and papers on file, to-wit:

1. Writ of error.
2. Citation on writ of error and acknowledgment of service.
3. Petition for removal.
4. Notice of motion for hearing petition for removal.
5. Bond on removal.
6. Order removing case.
7. Complaint.
8. Demurrer to complaint.

9. Notice of motion to strike from complaint.
10. Minute order of July 31, 1922, sustaining defendant's demurrer.
11. Amendment to complaint.
12. Demurrer to amended complaint.
13. Minute order of Nov. 6, 1922, overruling demurrer to amended complaint.
14. Answer to first cause of action.
15. Answer to second cause of action.
16. Supplemental answer.
17. Minute order of March 19, 1923, allowing filing of Supplemental Answer.
18. Stipulation waiving trial by jury.
19. Minute order of court entered August 13, 1924.
20. Findings of fact and conclusions of law.
21. Objections to findings.
22. Judgment.
23. Opinion filed August 13, 1924.
24. Memorandum supplemental to Opinion filed Nov. 28, 1924.
25. Memorandum supplemental to opinion filed Feb. 23, 1925.
26. Minute order of February 23, 1925.
27. Bill of exceptions including order allowing same, and affidavit of Dale H. Parke, and affidavit of T. B. Cosgrove.
28. Stipulation filed and order entered March 13, 1925, extending time within which defendant might file bill of exceptions.



29. Stipulation filed and order entered on April 14, 1925, extending time within which defendant might prepare and file bill of exceptions.

30. Stipulation filed and order entered on May 15, 1925, extending time within which defendant might prepare and file bill of exceptions.

31. Stipulation entered into on the 9th day of June, 1925, extending time within which plaintiff might propose amendments to bill of exceptions.

32. Notice of presentation of Bill of Exceptions for settlement.

33. Petition for writ of error.

34. Assignments of error. (attached to petition for writ)

35. Order allowing writ of error and supersedeas.

36. Receipt by attorneys for plaintiff of order allowing writ and of assignments of error.

37. Bond on writ of error and supersedeas.

38. Order extending time within which plaintiff in error might file record and docket the case, Circuit Court of Appeals.

39. This praecipe.

Said transcript to be prepared as required by law and the rules of said court, and the rules of the United States Circuit Court of Appeals for the Ninth Circuit, and filed in the office of the clerk of the United States Circuit Court of Appeals before the 4th day of September, A. D. 1925.

Dated: Los Angeles, California, this 3d day of August, 1925.

MARYLAND CASUALTY COMPANY,  
A CORPORATION

Plaintiff in Error

By Bicksler, Smith & Parke

Attorneys for said plaintiff in error

[Endorsed]: No. 1124-Civil In the UNITED STATES DISTRICT COURT In and for the Southern District of California, SOUTHERN DIVISION In the Matter of Citizens Nat. Bk. of L. A., Plaintiff vs. Maryland Casualty Co., Defendant AMENDED PRAECIPE FOR TRANSCRIPT OF RECORD Received copy of the within amended praecipe this 7th day of Aug 1925 Hunsaker, Britt & Cosgrove attorney for Deft-in-Error FILED AUG 7 1925 CHAS. N. WILLIAMS, Clerk By L J Cordes Deputy Clerk BICKSLER, SMITH & PARKE 829 Citizens Nat'l Bank Bldg., Fifth & Spring Sts. Los Angeles, Cal. Telephone TRinity 4331 Attorneys for defendant

IN THE UNITED STATES DISTRICT COURT  
IN AND FOR THE SOUTHERN DISTRICT  
OF CALIFORNIA SOUTHERN  
DIVISION

THE CITIZENS NATIONAL	)	
BANK OF LOS ANGELES,	)	No. 1124-Civil
	)	
Plaintiff	)	
vs	)	CLERK'S
	)	CERTIFICATE.
MARYLAND CASUALTY	)	
COMPANY, a Corporation,	)	
	)	
Defendant.	)	

I, CHAS. N. WILLIAMS, Clerk of the United States District Court for the Southern District of California, do hereby certify the foregoing volume containing 549 pages, numbered from 1 to 549 inclusive, to be the Transcript of Record on Writ of Error in the above entitled cause, as printed by the plaintiff-in-error, and presented to me for comparison and certification, and that the same has been compared and corrected by me and contains a full, true and correct copy of the writ of error, citation on writ of error and acknowledgment of service, petition for removal, notice of motion for hearing petition for removal, bond on removal, order removing case, complaint, demurrer to complaint, notice of motion to strike from complaint, minute order of July 31, 1922, sustaining defendant's demurrer, amendment to complaint, demurrer to amended complaint, minute order of Nov. 6,

1922, overruling demurrer to amended complaint, answer to first cause of action, answer to second cause of action, supplemental answer, minute order of March 19, 1923, allowing filing of supplemental answer, stipulation waiving trial by jury, minute order of court entered August 13, 1924, findings of fact and conclusions of law, objections to findings, judgment, opinion filed August 13, 1924; memorandum supplemental to opinion filed Nov. 28, 1924; memorandum supplemental to opinion filed Feb. 23, 1925; minute order of February 23, 1925; bill of exceptions including order allowing same, and affidavit of Dale H. Parke, and affidavit of T. B. Cosgrove; stipulation filed and order entered March 13, 1925, extending time within which defendant might file bill of exceptions; stipulation filed and order entered on April 14, 1925, extending time within which defendant might prepare and file bill of exceptions; stipulation filed and order entered on May 15, 1925, extending time within which defendant might prepare and file bill of exceptions; stipulation entered into on the 9th day of June, 1925, extending time within which plaintiff might propose amendments to bill of exceptions; notice of presentation of bill of exceptions for settlement; petition for writ of error; assignments of error; order allowing writ of error and supersedeas; receipt by attorneys for plaintiff of order allowing writ and of assignments of error; bond on writ of error and supersedeas and praecipe.



I DO FURTHER CERTIFY that the fees of the Clerk for comparing, correcting and certifying the foregoing Record on Writ of Error amount to..... and that said amount has been paid me by the plaintiff-in-error herein.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the Seal of the District Court of the United States of America, in and for the Southern District of California, Southern Division, this.....day of August, in the year of Our Lord One Thousand Nine Hundred and Twenty-five, and of our Independence the One Hundred and Fiftieth.

CHAS. N. WILLIAMS,

Clerk of the District Court of the  
United States of America, in  
and for the Southern District  
of California.

By

Deputy. 51









